85-568 (2)

No. 85-

IN THE

Supreme Court of the United States

OCTOBER TERM, 1985

NANTAHALA POWER AND LIGHT COMPANY,
TAPOCO, INC., and
ALUMINUM COMPANY OF AMERICA,

Appellants,

v.

STATE OF NORTH CAROLINA ex rel.
UTILITIES COMMISSION; LACY H.
THORNBURG, Attorney General,
et al.,

Appellees.

On Appeal from the Supreme Court
of North Carolina

APPENDIX TO JURISDICTIONAL STATEMENT

REX E. LEE*
DAVID W. CARPENTER
SIDLEY & AUSTIN
1722 Eye St., N.W.
Washington, D.C. 20006
(202) 429-4000
Counsel for Appellants

Of Counsel:
RONALD D. JONES
DAVID R. POE
M. REAMY ANCARROW
LEBOEUF LAMB, LEIBY & MACRAE

EDWARD S. FINLEY, JR.
WILLIAM D. JOHNSON
GRADY L. SHIELDS
HUNTON & WILLIAMS

Counsel of Record

3561

TABLE OF CONTENTS

	PAGE
Appendix A—Opinion Of The North Carolina Supreme Court	1a
Appendix B—Opinion Of The North Carolina Court of Appeals	141a
Appendix C—Opinion Of The North Carolina Utilities Commission, dated September 2, 1981	165a
Appendix D—Opinion Of The North Carolina Utilities Commission, dated January 28, 1982	236a
Appendix E—Excerpts From The Federal Power Act, 16 U.S.C. §§791a-828c	248a
Appendix F—Excerpts From The North Carolina Public Utilities Act, N.C. Gen. Stat. §§62-1, *et seq.*	258a
Appendix G—Opinion Of FERC In *Tapoco, Inc.*, Docket No. ER81-19-000	262a
Appendix H—Excerpts From Administrative Law Judge Decision, *Nantahala Power and Light Company*, Docket No. ER76-828; *Town of Highlands, North Carolina* v. *Nantahala Power and Light Company*, Docket No. EL78-18	267a
Appendix I—Excerpts From FERC Opinion No. 139, *Nantahala Power and Light Company*, Docket No. ER76-828-000; *Town of Highlands, North Carolina* v. *Nantahala Power and Light Company*, Docket No. EL78-18-000	283a

	Page
Appendix J—Excerpts From FERC Opinion No. 139-A, *Nantahala Power and Light Company*, Docket Nos. ER76-828-002,-003,-004, -005; *Town of Highlands, North Carolina* v. *Nantahala Power and Light Company*, Docket Nos. EL78-18-002,-003,-004, -005	302a
Appendix K—Notices Of Appeal	314a
Appendix L—Opinion Of The Eighth Circuit In *Middle South Energy, Inc. v. Arkansas Public Service Commission*, Nos. 84-2409, 84-?410, and 84-2480 (filed Aug. 23, 1985)	319a
Appendix M—Supplement To Rule 28.1 Statement	345a

APPENDIX A

Opinion Of The North Carolina Supreme Court

STATE OF NORTH CAROLINA, EX REL. UTILITIES COMMISSION; RUFUS L. EDMISTEN, ATTORNEY GENERAL; PUBLIC STAFF; HENRY J. TRUETT; TOWN OF BRYSON CITY; SWAIN COUNTY BOARD OF COUNTY COMMISSIONERS; CHEROKEE, GRAHAM AND JACKSON COUNTIES, THE TOWNS OF ANDREWS, DILLSBORO, ROBBINSVILLE, AND SYLVA; THE TRIBAL COUNCIL OF THE EASTERN BAND OF CHEROKEE INDIANS; MURIEL MANEY; AND DEROL CRISP v. NANTAHALA POWER AND LIGHT COMPANY; ALUMINUM COMPANY OF AMERICA; AND TAPOCO, INC.

No. 227A83

(Filed 3 July 1985)

1. Electricity § 3; Utilities Commission § 36— electric rates—affiliated utilities—treatment as integrated system—authority of Utilities Commission

The Utilities Commission has the authority, in the first instance, to determine for itself the relevant criteria to apply to the factual question of whether to treat Nantahala Power Company and Tapoco, Inc. as an integrated system for rate making purposes, and its determination will not be disturbed on appeal where supported by substantial evidence.

2. Electricity § 3; Utilities Commission § 15— Tapoco as public utility

The Utilities Commission correctly determined that Tapoco, Inc. is a public utility in North Carolina subject to its regulatory authority and jurisdiction.

3. Appeal and Error § 2— unanimous decision of Court of Appeals—scope of review

Pursuant to Rule 16(a) of the Rules of Appellate Procedure, the scope of review in the Supreme Court from an unanimous decision of the Court of Appeals is limited to consideration of the questions properly presented in the new briefs required by Rule 14(d)(1) and 15(g)(2) to be filed in the Supreme Court. Questions properly presented for review in the Court of Appeals but not presented and discussed in the new briefs to the Supreme Court are deemed abandoned under Rule 28(a).

4. Electricity § 3; Utilities Commission § 36— electric rates—roll-in methodology for Nantahala—no preemption by federal license

The Utilities Commission's order implementing a roll-in of the properties, revenues and expenses of Tapoco with those of Nantahala for the purpose of setting Nantahala's retail rates in no way contravened the terms and conditions of Tapoco's federal license to operate hydroelectric plants in North Carolina and Tennessee, and the Commission was not, therefore, preempted from implementing the roll-in by virtue of Part I of the Federal Power Act and the Supremacy Clause, Art. VI, cl. 2, of the U.S. Constitution.

5. Electricity § 3; Utilities Commission § 36— electric rates—affiliated utilities—treatment as integrated system—sufficient evidence

There was plenary evidence in the record to support a determination by the Utilities Commission that Nantahala and Tapoco constitute a single, in-

tegrated electric system and should be treated as such for the purposes of calculating Nantahala's retail rate base and costs of service.

6. Electricity § 3; Utilities Commission § 15— Alcoa as public utility

The evidence supported a determination by the Utilities Commission that Alcoa, the owner of all of the outstanding stock of Nantahala Power Company, is a North Carolina public utility under G.S. 62-3(23)c by virtue of the effect Alcoa's "affiliation" with Nantahala has had upon Nantahala's rates.

7. Electricity § 3; Utilities Commission § 36— electric rates—roll-in methodology for Nantahala—no preemption by Federal Power Act and Supremacy Clause

The Utilities Commission was not preempted from implementing a roll-in methodology for determining Nantahala's rates by virtue of the Supremacy Clause, Art. VI, cl. 2, of the U.S. Constitution and the Federal Energy Regulatory Commission's exclusive jurisdiction under Part II of the Federal Power Act over certain wholesale power transactions and agreements between and among Nantahala, Tapoco, Alcoa and TVA. The "filed rate" doctrine did not require the Utilities Commission, in determining the proper costs to Nantahala's retail customers for the service provided to them, to use demand and energy factors based upon the proportion of entitlements allocated to Nantahala alone under such agreements. Nor did the Utilities Commission's order conflict with specific FERC actions taken with respect to such agreements.

8. Electricity § 3; Utilities Commission § 21— jurisdiction over intrastate and interstate rates

The Federal Energy Regulatory Commission is prohibited from regulating intrastate retail rates charged to ultimate consumers, and the states are prohibited from regulating interstate wholesale rates charged to local distributing companies.

9. Electricity § 3; Utilities Commission § 21— wholesale intrastate electric rates—no authority by Utilities Commission

The N.C. Utilities Commission was preempted from directly or indirectly regulating the wholesale rate structure created by certain interstate power agreements between and among Nantahala, Tapoco, Alcoa and TVA or inquiring into the reasonableness of those FERC-filed wholesale rate schedules when it acted in fixing Nantahala's retail rates.

10. Utilities Commission § 38— electric rates—operating expenses considered

When the provisions of G.S. 62-133(b)(1), (b)(3) and (c) are read *in pari materia*, the only operating expenses which the Utilities Commission may consider in setting intrastate rates for North Carolina public utilities are those incurred in the provision of service to the utility's North Carolina consumers. Accordingly, jurisdiction cost allocation is a necessary step in any general rate case involving a public utility or utility system whose separate companies are operated as a single enterprise serving both jurisdictional (intrastate retail) and non-jurisdictional consumers.

11. Utilities Commission § 24— fixing "reasonable and just" rates—balancing of shareholder and consumer interests

The fixing of "reasonable and just" rates involves a balancing of shareholder and consumer interests. The Utilities Commission must therefore set rates which will protect both the right of the public utility to earn a fair rate of return for its shareholders and ensure its financial integrity while also protecting the right of the utility's intrastate customers to pay a retail rate which reasonably and fairly reflects the cost of service rendered on their behalf.

12. Utilities Commission § 38— operating expenses—questions of fact

The fundamental question as to whether certain expenditures are to be included in the operating expenses a utility is entitled to collect from its customers is one of fact to be ascertained by the regulatory authority.

13. Electricity § 3; Utilities Commission § 36— electric rates—power costs paid to affiliate

Ordinarily, the Utilities Commission may, in a proper case, refuse to allow a utility to include in its reasonable operating expenses the full price it actually paid for power as a result of its contractual power supply arrangements, especially where the operating expense is one incurred through a contract between or including the utility company and its affiliated companies. In such cases, the burden of persuasion on the issue of reasonableness always rests with the utility, and charges arising out of intercompany relationships between affiliated companies should be scrutinized with care and may be properly refused or disallowed in the absence of a showing of their reasonableness.

14. Electricity § 3; Utilities Commission § 36— electric rates—transactions with affiliated companies—filed rate doctrine

The Utilities Commission's otherwise plenary authority to investigate transactions between a public utility and its affiliated companies, and to disallow operating expenses found to be imprudently incurred or allocated under such agreements, is limited by prior federal approval of the rate or price in question under the "filed rate" doctrine. Thus, neither the state public service commission nor the courts can unilaterally establish a different rate for wholesale electric power sold in interstate commerce because they are of the opinion that an FERC-filed or approved rate is unfair or unreasonable.

15. Electricity § 3; Utilities Commission § 36— Nantahala's retail rates—interstate power supply arrangements—benefits to Alcoa—costs to be borne by Alcoa

Insofar as the Utilities Commission determined that Alcoa, as corporate parent and private industrial customer of Nantahala Power Company, had benefited at the expense of Nantahala's public load from interstate corporate and power supply arrangements it imposed upon its subsidiaries, it was within its regulatory authority to decide that the costs associated with those benefits would not be borne by Nantahala's public consumers in the form of higher retail rates but would be borne by Nantahala's customer and sole shareholder, Alcoa.

16. Electricity § 3; Utilities Commission § 36— electric rates—demand and energy factors—failure to use entitlements under interstate agreements—filed rate doctrine

The "filed rate" doctrine did not require the Utilities Commission, in determining the proper costs to Nantahala's retail customers for the service provided to them, to use demand and energy factors based upon the proportion of entitlements allocated to Nantahala alone under certain interstate wholesale power agreements between and among Nantahala, Tapoco, Alcoa and TVA.

17. Electricity § 3; Utilities Commission § 36— Alcoa's dominance of Nantahala—roll-in methodology—effect of FERC actions

The Federal Energy Regulatory Commission's analysis of the corporate structure of Alcoa, Nantahala and Tapoco and various intercorporate power transactions and agreements, and its finding that the evidence before it did not support the conclusion that Alcoa had used the separate corporate identities of Nantahala and Tapoco to frustrate the purposes of the Federal Power Act, did not preempt the N.C. Utilities Commission from determining that the evidence before it supported the conclusion that Alcoa had dominated Nantahala in such a manner as to require relief for Nantahala's retail customers under N.C. law. Nor did the Federal Energy Regulatory Commission's having declined to order a roll-in of Nantahala and Tapoco for rate making purposes preempt the Utilities Commission from implementing such a rate making methodology under its discretionary authority in setting intrastate retail rates.

18. Electricity § 3; Utilities Commission § 36— electric rates—roll-in methodology—no undue burden on interstate commerce

The Utilities Commission's adoption of a roll-in of the properties, revenues and expenses of Tapoco with those of Nantahala for the purpose of setting Nantahala's retail rates did not afford N.C. customers a "first call" on the energy output of the combined system and the economic benefits of Tapoco's lower-cost production so as to place an undue burden on interstate commerce in violation of the Commerce Clause, Art. I, § 8, cl. 3, of the U.S. Constitution.

19. Electricity § 3; Utilities Commission § 36— electric rates—roll-in methodology—no confiscation of Nantahala's properties

The Utilities Commission's implementation of a roll-in methodology for setting Nantahala's retail rates, with its resulting reduction in retail rates and refund obligation to Nantahala's retail customers, does not impermissibly impair Nantahala's ability to earn a proper rate of return on its investment and does not amount to a confiscation of its properties in violation of the due process clause of the Fourteenth Amendment to the U.S. Constitution and Art. I, § 19 of the N.C. Constitution.

20. Electricity § 3; Utilities Commission § 36— requiring refund to Nantahala's customers by Alcoa—authority of Utilities Commission

The Utilities Commission acted within its regulatory and rate making authority in imposing the obligation upon Nantahala's parent Alcoa to pay any portion of a refund obligation to Nantahala's retail customers which Nantahala is financially unable to pay. Once the Utilities Commission determined that

Alcoa was a statutory public utility under G.S. 62-3(23)c, it could rely upon the doctrine of "piercing the corporate veil" between Nantahala and its parent, Alcoa, to hold Alcoa financially responsible for Nantahala's refund obligation to the extent its affiliation had adversely affected Nantahala's rates as necessary or incident to the proper discharge of its regulatory duties under G.S. 62-30.

21. Electricity § 3; Utilities Commission § 36— electric rates—piercing the corporate veil—fraud not required

The Utilities Commission was not required to find fraud in order to pierce the corporate veil between Nantahala and its parent, Alcoa.

22. Electricity § 3; Utilities Commission § 36— Nantahala's retail rates—piercing the corporate veil—effect of prior actions by regulatory agencies

Prior investigation and regulation of the activities of Alcoa and Nantahala by state and federal regulatory agencies did not prohibit or preempt the N.C. Utilities Commission from piercing the corporate veil between Alcoa and its wholly-owned subsidiary Nantahala to hold Alcoa financially responsible for Nantahala's refund obligation to its retail customers.

23. Electricity § 3; Utilities Commission § 36— refund to Nantahala's customers—responsibility of Alcoa

There was no merit to Alcoa's contention that it could not be required to pay refunds based upon Nantahala's overcollections prior to 30 October 1980, the date on which the Utilities Commission found Alcoa to be a public utility.

24. Electricity § 3; Utilities Commission § 36— refund to Nantahala's customers—responsibility of Alcoa—no confiscation of Alcoa's property

The Utilities Commission's imposition of an obligation upon Alcoa to pay any portion of a refund obligation to Nantahala's retail customers which Nantahala is financially unable to pay does not amount to a confiscation of Alcoa's property.

25. Electricity § 3; Utilities Commission § 21— period of refund of excessive rates—no retroactive rate making

When, upon appellate review and further action by the Utilities Commission, rates approved for Nantahala by the Utilities Commission in 1977 were determined to be excessive, the Utilities Commission properly ordered Nantahala to refund all excessive rates collected since the 1977 order, not just overcollections which were subject to an undertaking for refund after 6 March 1979 when the Court of Appeals vacated the 1977 order. Furthermore, the Commission's refund order did not amount to retroactive rate making since the rates ultimately fixed and the refund were not collectible for past service but for service in the locked-in docket period.

26. Electricity § 3; Utilities Commission § 21— amount of refund to utility's customers

The Utilities Commission properly ordered Nantahala to refund excess revenue measured by rates determined by a roll-in methodology in this proceeding rather than by what would have been collected under Nantahala's prior rate schedule.

27. Electricity § 3; Utilities Commission § 56— electric rates—order based on independent findings

In this rate case in which the Utilities Commission implemented a roll-in methodology for determining Nantahala's rates and held Nantahala's parent corporation Alcoa financially responsible for refunds to Nantahala's customers, all parties received a full and fair hearing at all stages of the original and remanded proceedings, and the Commission's order was, in all respects, based upon fully independent and well substantiated findings of fact and conclusions of law and not on observations made by the N.C. Supreme Court in remanding the proceeding to the Commission.

Justice VAUGHN did not participate in the consideration or decision of this case.

APPEAL by respondents pursuant to N.C.G.S. § 7A-30(3) from the decision of the Court of Appeals, reported at 65 N.C. App. 198, 309 S.E. 2d 473 (1983), affirming the order of the North Carolina Utilities Commission entered 2 September 1981, Docket No. E-13, Sub 29 (Remanded) reducing retail electric utility rates and requiring a refund by respondents Nantahala Power and Light Company ("Nantahala") and its parent corporation, Aluminum Company of America ("Alcoa") to Nantahala's retail ratepayers for the four-year period of 1977-1981. Heard in the Supreme Court 12 April 1984.

This matter was initiated by Nantahala on 3 November 1976 by the filing of an application with the North Carolina Utilities Commission ("Commission") by Nantahala to establish new rates so as to increase its charges to North Carolina retail customers by $1,830,791. The Commission declared the matter to be a general rate case pursuant to N.C.G.S. § 62-137 and ordered an investigation and hearing. Various parties representing the interests of Nantahala's retail ratepayers intervened and moved that Alcoa and its wholly-owned subsidiary, Tapoco, Inc. ("Tapoco") be joined as parties and that the rate base of Nantahala be computed on a "rolled-in" basis to include the properties, revenues and expenses of Tapoco, as if the two were operating as one utility for the purpose of fixing and establishing a reasonable level of retail rates for Nantahala. These motions were disallowed by the Commission.

On 14 June 1977 the Commission issued an order in Docket No. E-13, Sub 29, permitting Nantahala to put into effect revised rates so as to produce $1,598,918 in additional gross revenues.

The order was not stayed and Nantahala implemented the approved rates at that time. The Court of Appeals reversed, held Tapoco to be a North Carolina public utility, vacated the order authorizing the rate increase and remanded the case to the Commission for the purpose of making Tapoco a party and considering "whether the people of North Carolina would benefit by the use of the roll-in method of rate making involving Nantahala and Tapoco." *Utilities Comm. v. Edmisten, Attorney General,* 40 N.C. App. 109, 120, 252 S.E. 2d 516, 522 (1979).

Nantahala sought and obtained from this Court a stay of the Court of Appeals' decision pending further review. Upon Nantahala's appeal from the Court of Appeals, this Court affirmed in part, reversed in part, and remanded the matter to the Commission for further hearings. *Utilities Comm. v. Edmisten, Attorney General,* 299 N.C. 432, 263 S.E. 2d 583 (1980) ("*Edmisten*").

In *Edmisten* we assumed, without deciding, that Tapoco was a North Carolina public utility subject to the regulatory authority of the Commission, found that there was ample evidence to support a finding that Nantahala and Tapoco operate as a single unified public utility system, held that the Commission erred in giving only minimal consideration to the evidence suggesting the propriety of roll-in, and indicated that the roll-in device or methodology for rate making computation "seems especially appropriate in a case such as this where one physically integrated system, interconnected in such a way that all power available to the system can be used to enhance its overall reliability and supply its requirements as a whole, is presided over by two corporate entities." 299 N.C. at 442, 263 S.E. 2d at 591. In addition, this Court held that Alcoa and Tapoco could be brought in as parties, with a *de novo* right to contest the Commission's jurisdiction; permitted the increased rates to remain in effect, conditioned upon Nantahala's guarantee that it would refund to its customers any excess charges, should the increased rates originally approved by the Commission ultimately be determined to be excessive; and remanded the matter to the Commission with directions to "obtain and consider information and data showing what Nantahala's cost of service to its customers would be if this [roll-in] method of rate making were used and whether Nantahala's customers would benefit thereby." 299 N.C. at 443, 263 S.E. 2d at 591. Thereafter, Nantahala executed an Undertaking to Refund, agreeing to re-

fund any overcollections to its customers should the rates approved by the order of 14 June 1977 be determined excessive.

Upon remand to the Commission and after *de novo* proceedings, Alcoa and Tapoco were held to be North Carolina public utilities and both were made parties respondent to the proceeding. Prior to the remanded rate hearings, the intervenors moved that Alcoa and Tapoco be required to join the execution of Nantahala's undertaking, or, in the alternative, to guarantee Nantahala's ability to make the refund. The Commission deferred its ruling on this motion until a later date.

The case was heard before a panel of the Commission during the months of March, April and May of 1981, and both the intervenors and the respondents presented evidence concerning the propriety of a roll-in, for accounting purposes, of Nantahala's and Tapoco's accounting data in setting Nantahala's retail rates. The panel determined that Nantahala's retail customers would benefit by a roll-in methodology treating Nantahala and Tapoco as a unified system and adopted the roll-in cost allocation formula proposed by the intervenors. On 2 September 1981 the panel ordered a reduction in Nantahala's rates from the level previously approved by the Commission's order of 14 June 1977, in the amount of $2,035,000 annually and, in addition, modified certain purchased power adjustment costs. The panel, consistent with the rate reduction, also ordered Nantahala to refund the excess rates it had been collecting under the 1977 order from its retail customers and directed that Alcoa would be responsible for refunding such portions of the total refund obligation as Nantahala itself is financially unable to refund.

The respondent companies appealed to the Full Commission. After additional hearings, the Commission affirmed and adopted the panel's order in all respects on 28 January 1982. On 16 August 1982, the Commission, after requesting and rejecting several refund plans submitted by Nantahala and Alcoa, ordered the two companies to commence making refunds by monthly installments in October 1982. The Commission left it to the companies to determine the proportion of the refund obligation each would pay, with the provision that any division of financial responsibility not affect Nantahala's ability to continue service to its customers.

The Commission's order was stayed pending appeal to the Court of Appeals. Thereafter, all relevant orders of the Commission were affirmed by the Court of Appeals in *State ex rel. Utilities Comm. v. Nantahala Power & Light Co.*, 65 N.C. App. 198, 309 S.E. 2d 475 (1983). The respondents appeal pursuant to former N.C.G.S. § 7A-30(3), which permitted an appeal of right of any general rate case from the Court of Appeals to this Court in cases decided prior to 1 July 1983. *See* 1983 N.C. Session Laws, Ch. 526, Sec. 10.

Hunton & Williams, by Robert C. Howison, Jr., and Edward S. Finley, Jr., Attorneys for defendant-appellant Nantahala Power and Light Company.

LeBoeuf, Lamb, Leiby & MacRae, by Ronald D. Jones and David R. Poe, Attorneys for respondent-appellants Aluminum Company of America and Tapoco, Inc.

Rufus L. Edmisten, Attorney General, by Richard L. Griffin, Assistant Attorney General, Attorney for Using and Consuming Public.

Robert Gruber, Executive Director, by James D. Little, Staff Attorney, The Public Staff, Attorneys for Using and Consuming Public.

Crisp, Davis, Schwentker & Page, by William T. Crisp and Robert W. Schwentker, Attorneys for Henry J. Truett; Counties of Cherokee, Graham, Swain, Jackson; Towns of Andrews, Dillsboro, Robbinsville, Bryson City, Sylva; and the Tribal Council of the Eastern Band of the Cherokee Indians.

Joseph A. Pachnowski, Attorney for the County of Swain and the Town of Bryson City.

Western North Carolina Legal Services, by Larry Nestler, Attorney for Derol Crisp.

McKeever, Edwards, Davis & Hays, by Fred H. Moody, Jr., Attorney for County of Swain.

Charles L. Lewis, Assistant Attorney General, Attorney for State of Tennessee and Tennessee Department of Economic and Community Development, Amici Curiae.

Mayer & Magie, by Roderic G. Magie, and Spiegel & McDiarmid, by James N. Horwood, Cynthia S. Bogorad, and P. Daniel Bruner, Attorneys for the Town of Highlands, Amicus Curiae.

MEYER, Justice.

TABLE OF CONTENTS

Preliminary Matters

I

A. Procedural Background

B. Historical Development of the Unified Nantahala-Tapoco System

C. Factual Predicates of the Roll-In

1. Public Utility Status of Tapoco

2. Nantahala and Tapoco as a Unified System

3. Public Utility Status of Alcoa

D. Mechanics of the Roll-In in the Allocation of System Costs

II

A. Federal Preemption

1. Federal Power Act; "Filed Rate" Doctrine

2. Federal Regulatory Actions

B. Interference with Interstate Commerce

C. Rate Reduction and Refund Obligation

1. Nantahala's Constitutional Challenges

a. Reduced Rates as Confiscatory

b. Refund Obligation as Confiscatory

2. Alcoa's Challenges; Liability

a. Statutory Powers of the Commission

b. Legal and Factual Basis for Alcoa's Refund Liability

c. Preemptive Effect of Federal Regulation

d. Refund Required

1. Temporal Extent

2. Confiscation

3. Nantahala's Non-Constitutional Challenges

a. Temporal Extent of Refund Obligation

b. Measure of Refund Obligation

D. Independent Findings of the Commission

III

Conclusion and Holding

This appeal raises substantial questions under the federal constitution and the North Carolina statutory provisions governing intrastate electric power rates charged by a public utility to its retail customers. The most important question presented is whether the North Carolina Utilities Commission is preempted from implementing a roll-in methodology for setting Nantahala's retail rates by virtue of the Supremacy Clause of the United States Constitution, art. VI, cl. 2 and the Federal Energy Regulatory Commission's ("FERC") exclusive jurisdiction over certain interstate wholesale power transactions and agreements[1] between and among, Nantahala, Tapoco, Alcoa and the Tennessee Valley Authority ("TVA"). For the reasons set forth more fully below, we find no statutory or constitutional infirmity in the order of the North Carolina Utilities Commission issued in Docket No. E-13, Sub 29 (Remanded), and therefore affirm the decision of the Court of Appeals upholding the retail rate reduction and refund obligation to Nantahala's public utility customers.

In Part I of this opinion we will undertake to review (a) the procedural history of this case, (b) the historical development of Nantahala and Tapoco as a single, unified hydroelectric generating and distribution system, (c) the factual predicate to the Commission's decision to implement a roll-in rate making methodology, and (d) the mechanics of the roll-in in the allocation of costs for the unified system. In the course of this review, we shall address such factual and legal issues raised by the companies as are relevant to the Commission action under discussion. In Part II, we will address the major constitutional and statutory challenges to the Commission's order lodged by the respondent companies. Briefly stated, these challenges concern (a) federal preemption; (b) interference with interstate commerce; (c) the measure, extent and liability for the rate reduction and refund obligation; and (d) the independence of the factual findings of the Commission.

1. Part II of the Federal Power Act, 16 U.S.C. §§ 824-824k extends federal regulatory power to the transmission and sale of electric energy at wholesale in interstate commerce, while reserving to the various states the authority to regulate intrastate transmission and sale of electric energy at retail.

I.

A.

This appeal represents the culmination of a process begun in 1976, with Nantahala's application for permission to increase its retail rates and a revision of its purchased power adjustment clause (PPAC) applicable to those rates. The initial order entered by the Commission on 14 June 1977 in Docket No. E-13, Sub 29, approving certain annual increases in Nantahala's rates and a PPAC adjustment was ultimately reversed on appeal by this Court in *Edmisten*, 299 N.C. 432, 263 S.E. 2d 583. The basis for reversal was the Commission's failure as a matter of law to give more than minimal consideration to material facts of record concerning the propriety of treating Nantahala and its affiliate Tapoco, both wholly owned subsidiaries of Alcoa, as a single unified electric utility and rolling together their properties and costs for purposes of determining just and reasonable retail electric rates for Nantahala's North Carolina customers. 299 N.C. at 437, 263 S.E. 2d at 587-88. The case was remanded with directions to the Commission to obtain and consider information and data showing what Nantahala's cost of service to its customers would be if the roll-in method of rate making were used and whether Nantahala's customers would benefit thereby. *Id.* at 443, 263 S.E. 2d at 591.

Upon remand, the Commission, in preliminary hearing, determined that it had jurisdiction over Nantahala's parent corporation, Alcoa and its affiliate, Tapoco, and joined them as parties in Docket No. E-13, Sub 29 (Remanded). A panel of the Full Commission then held hearings and received evidence from both the intervening customers of Nantahala and from the respondent com-

panies on the question of roll-in. In addition to the evidence received during Nantahala's initial rate increase hearings in 1977 regarding Nantahala's costs and the relevant test year (1975) data, both parties presented additional testimony and data concerning Nantahala's rolled-in costs of service to its retail customers. The companies presented one allocation methodology for apportioning the combined revenues, expenses and investment of the rolled-in system between the system's North Carolina retail operations and non-jurisdictional Tennessee industrial operations, and the intervenors presented another.

Briefly stated, the basic dispute between the intervenors and the companies as to *which* jurisdictional cost allocation methodology to use involves the question of whether the rolled-in power costs are to be allocated to Nantahala's retail customers on the basis of its actual contribution and use of hydroelectric generation and capacity in the unified system or upon the proportion of return power entitlements it receives under the wholesale agreements between and among the companies themselves and the Tennessee Valley Authority ("TVA"). The intervenors contend that the former allocation formula is just and appropriate for setting Nantahala's retail rates. The companies maintain that the latter is mandated under the federal and state division of, respectively, wholesale and retail rate making authority, because the contracts at issue are federally filed and approved wholesale rates which must be given effect by state public service commissions in setting retail rates.

The wholesale power coordination and exchange agreements primarily at issue are (1) the New Fontana Agreement ("NFA"), a 1962 power exchange agreement among the three companies and TVA, whereby Nantahala and Tapoco subject all of their large plant electrical generation to TVA control and turn over that generation directly to TVA, in exchange for annual return power entitlements for the two subsidiaries to divide amongst themselves; and (2) the 1971 Nantahala-Tapoco Apportionment Agreement, a contract between the two subsidiaries, whereby the demand and energy return power entitlements received under the NFA are divided between them, with Nantahala receiving no more than a fixed amount of power and energy, and Tapoco receiving the re-

mainder.[2] These, and other contractual arrangements affecting Nantahala's costs of service will be discussed more fully below.

The Commission, in view of the evidence presented by all the parties upon remand, found and concluded that (1) Nantahala and Tapoco are North Carolina public utilities subject to its rate making jurisdiction; (2) Alcoa, by virtue of its parental domination of Nantahala, was itself a statutory North Carolina public utility pursuant to N.C.G.S. § 62-3(23)c; (3) the Nantahala-Tapoco electric generation and distribution system constitutes a single, integrated electric system, operated as such and coordinated with the TVA system; (4) use of an appropriately performed roll-in of Nantahala and Tapoco would be beneficial to Nantahala's customers because its allocated cost of power under the combined system is less than the cost of power for Nantahala as a stand-alone system, such that a roll-in will result in a significant reduction in the cost of providing public utility electric service to the single system's retail customers; (5) significant detriments and inequities to Nantahala arise out of both the NFA and the 1971 Apportionment Agreement, which result in concealed benefits flowing to Alcoa through its subsidiary Tapoco, and render use of the companies' cost allocation formula based on the demand and energy entitlements under those contracts inappropriate for determining the costs fairly attributable to the North Carolina public load in the combined system; (6) the cost allocation methods and procedures proposed by the intervenors, based upon the generational capabilities and needs of Nantahala, are proper for use in the allocation of its demand and energy related costs and should be adopted for use in setting Nantahala's retail rates in the subject proceeding; and (7) Alcoa had so dominated Nantahala in certain contracts and transactions involving Nantahala, Tapoco and others that Nantahala had been left "but an empty shell,

2. In practice, the NFA and its predecessor, the original Fontana Agreement ("OFA"), operated as "sales" to TVA of electric power for resale under Part II of the Federal Power Act, 16 U.S.C. §§ 824-824k, by Alcoa's subsidiary-public utilities (Nantahala and Tapoco), with TVA making payments in kind to the Alcoa "system" as a whole. In turn, TVA's "payments" of return power have been divided amongst the system members as they themselves have designated. The various agreements are, accordingly, treated as tariffs or rate schedules by FERC and are subject to regulation under Part II of the Act to assure that the terms and conditions are just and reasonable and not unduly discriminatory, despite the fact that no dollars actually change hands as rate payments.

unable to act in its own self-interest, let alone in the interest of its public utility customers in North Carolina," so as to render Alcoa responsible for such portions of any refund obligation placed upon Nantahala as Nantahala itself is unable to make.

The Commission adopted the intervenors' roll-in methodology, which resulted in lowered rates and required a refund obligation to be placed upon Nantahala and Alcoa. Essentially, the roll-in method adopted treats Nantahala and Tapoco as a single integrated system for accounting purposes. That is, (a) the assets, properties, plants and working capital requirements of the two companies were joined in one unified rate base; (b) the joint revenues and expenses of the single system were totalled; and (c) the combined system was assigned the rate of return previously approved by the Commission for Nantahala alone in the Sub 29 proceeding. From these three elements, the combined system revenue requirement (expenses + rate base × rate of return) was derived.

The combined system cost of service was then allocated between the public load customers in North Carolina and the industrial load customer (Alcoa) in Tennessee, using generally accepted jurisdictional allocation factors commonly employed by the Commission in setting North Carolina retail rates for other companies, such as Duke Power or Carolina Power & Light, which operate in more than one state. Rates for Nantahala's public load customers could be reduced because the cost of service per kwh for the combined Nantahala-Tapoco system is less than for Nantahala treated as a stand-alone electric system.

In its final order entered 28 January 1982, the Commission overruled the exceptions taken by the companies to the panel's order implementing roll-in and made supplementary conclusions of law on certain "federal questions" arising by virtue of the panel's rejection of the companies' proposed jurisdictional cost allocation methodology. The Commission rejected, inter alia, the companies' arguments (1) that the panel's order is precluded by exclusive federal licensing of interstate hydroelectric power facilities under Part I of the Federal Power Act, 16 U.S.C. §§ 791a-823a; (2) that the order intrudes upon the authority vested in FERC by Part II of the Federal Power Act, 16 U.S.C. §§ 824-824k, by failing to accept the costs of filed rates under the

NFA and the 1971 Apportionment Agreement; and (3) that the order imposes an impermissible burden on interstate commerce.

The companies, in their individual briefs, challenge the Commission's order on a number of state and federal grounds. Tapoco's sole contention relates to its "involuntary joinder" as a party on the grounds that the Commission is without statutory authority to affect Tapoco's rates and service to its Tennessee customer, Alcoa, and is preempted from doing so by virtue of the fact that Tapoco's four hydroelectric plants are licensed by, and under the exclusive regulatory jurisdiction of, FERC under Part I of the Federal Power Act, 16 U.S.C. §§ 791a-823a. Nantahala's and Alcoa's objections may be broken down into four categories: (1) challenges to the order implementing the roll-in arising under the Supremacy Clause of the United States Constitution, art. VI, cl. 2 and Part II of the Federal Power Act, 16 U.S.C. §§ 824-824k; (2) claims that the order contravenes the Commerce Clause of the United States Constitution, art. I, sec. 8, cl. 3, by placing an impermissible burden on interstate commerce; (3) challenges to the constitutionality, measure and extent of the rate reduction and refund obligation as well as to the Commission's jurisdiction to hold Alcoa liable for its subsidiary's refund obligation; and (4) challenges to the order issued on remand based upon the alleged failure of the Commission to make independent findings of fact as to the propriety of the roll-in methodology for determining Nantahala's rates and its jurisdiction over Nantahala's parent Alcoa.

In our earlier decision reversing the Commission's 1977 approval of the rate increase requested by Nantahala in Docket No. E-13, Sub 29, we briefly reviewed the history of the three companies and the basic contracts affecting Nantahala's costs of service. *Edmisten*, 299 N.C. at 434-39, 263 S.E. 2d at 586-89. That review was undertaken with an eye toward (1) elucidating the material facts of record accorded only minimal consideration by the Commission in assessing the factors bearing upon the determination of reasonable retail rates for Nantahala and (2) delineating the legal significance of evidence indicating that Nantahala had structured its economic affairs and physical operations so as to afford an unfair preference to its parent corporation to the detriment of its North Carolina public utility customers. *Id.* The complex factual predicate of the Commission's order implementing roll-in and the rather intricate corporate and contractual rela-

tionships between and among the companies and TVA renders a more extended treatment of the subject necessary in order to place the issues raised by the parties to the present appeal in their proper perspective.[3]

B.

As we noted in *Edmisten*, the factual background of the case is not generally disputed by the parties. In the early part of the century, Alcoa came to the sparsely populated southwestern North Carolina mountains to tap the resources of the mountain streams for low-cost electric power to operate an aluminum reduction plant in neighboring Alcoa, Tennessee. As its source of hydroelectric power, Alcoa acquired the Tallassee Power Company ("Tallassee") (later Carolina Aluminum Company and now Yadkin, Inc.), an electric generating company incorporated in North Carolina and granted the power of eminent domain by legislative act in 1905.[4] Tallassee owned several undeveloped and developed hydroelectric sites along the Little Tennessee River in North Carolina, including two hydroelectric generating facilities at Santeetlah and Cheoah. Tallassee, under the name Carolina Aluminum, was recognized as a North Carolina public utility as early as 1934 in *Manufacturing Co. v. Aluminum Co.*, 207 N.C. 52, 175 S.E. 698 (1934).

By the 1920's, Alcoa, through its subsidiaries, had acquired a substantial number of hydroelectric sites along the Little Tennessee River: Santeetlah, Cheoah, Nantahala, Glenville (now Thorpe), Needmore, Fontana and several smaller sites in North Carolina and Chilhowee and Calderwood in Tennessee. Development of the sites was primarily for the purpose of producing and transmitting electricity to the Alcoa, Tennessee aluminum reduction plant, which requires enormous amounts of low-cost electricity.

3. For the purposes of this historical review, we have relied upon the entire record before the Commission in the Sub 29 (Remanded) proceeding. In addition, in an effort to present a complete picture of the regulatory history of the companies involved, we have, where necessary, taken judicial notice of various prior opinions of this Court, as well as certain prior decisions and orders of the Federal Power Commission and its successor, the Federal Energy Regulatory Commission.

4. *See* Chapter 122 of the private laws enacted by the General Assembly of North Carolina at its regular session in the year 1905.

In 1929 Alcoa created and incorporated Nantahala as another of its wholly owned subsidiaries in North Carolina. Nantahala is a North Carolina public utility with the right of eminent domain, serving a six county franchised territory in the western part of the State. Nantahala's customer mix consists of residential, commercial, industrial and wholesale customers. In time, Tallassee sold its undeveloped North Carolina sites to Nantahala, including the Fontana site later developed by TVA. By 1939, Nantahala owned sites for power development in six western counties of North Carolina.

Between 1929 and 1941, Nantahala undertook token public service through several small, run-of-the-river hydroelectric generating plants acquired from municipalities in its service area and completed acquisition of several sites from Tallassee. In 1941 Nantahala obtained a certificate from the Department of War to develop the large-scale Nantahala and Glenville (now Thorpe) projects on the upper reaches of the Little Tennessee watershed. Nantahala's stated justification for the development of these sizeable projects was the huge electric need of Alcoa's aluminum smelting works in Tennessee, which were then producing aluminum to sell to the federal government for war materials. In its application, Nantahala repeatedly referred to the developments as part of "the Alcoa power system" or "the system."

Prior to 1941, both Nantahala and TVA were interested in developing the massive Fontana site on the Little Tennessee River in North Carolina. Nantahala proposed to construct a large hydroelectric project with storage capacity. The proposed project, known as the Fontana project, was to generate electricity both for aluminum production and for use by the public. Following a determination by FERC's predecessor, the Federal Power Commission ("FPC") that a license was required from that agency under Part I of the Federal Power Act before Nantahala could construct, thereby subjecting the proposed project and Nantahala to a limited-term license under Section 6 of the Act and to the agency's ongoing jurisdiction, Nantahala abandoned its proposal. *See Nantahala Power and Light Co.*, 2 F.P.C. 833 (1940), *petition for discontinuance denied*, 2 F.P.C. 388 (1941).[5] TVA, which had al-

5. Nantahala, upon learning that the project would not be exempt under federal law and that at most, the FPC would grant a 50-year license permitting

ready obtained some acreage in the reservoir site, eventually prevailed upon Alcoa to have the Fontana site transferred to TVA for development. At that time, Alcoa was already purchasing some of the power requirements for its Tennessee aluminum production facilities from TVA. The conveyance was part of the first power coordination and exchange agreement of relevance between Alcoa and TVA, entered into in 1941, which had become known over the years as the Original Fontana Agreement ("OFA").

The 1941 Agreement is a twenty-year (but annually renewable thereafter) contract between Alcoa and TVA, pursuant to which Alcoa agreed to cause Nantahala (not a party to the agree-

recapture, withdrew its declaration of intention. As to the companies' regard for the public's interests in this project, the Federal Power Commission stated:

> Notwithstanding the public interest, Alcoa, through its subsidiary, in effect demonstrated that in its national defense effort it was unwilling to accept the reasonable limitations on unearned increment in the value of its power project provided by Congress in the Federal Power Act.
>
> *The Fontana situation is not the only instance in which Alcoa and its subsidiaries have shown complete unwillingness to accept provisions of Federal law, regardless of the consequences to the national defense or to the public which they serve. . . .*
>
> Neither the Federal Power Act nor the licenses issued thereunder contain provisions onerous to the operation of a project utilizing the waters of streams subject to Federal control. The provisions of the Act and the license are, in fact, designed wholly to protect the public interest in the use of waters which belong to the Nation. Many other persons and corporations, both public utilities and industrial concerns, have sought and accepted licenses. *The refusal of Alcoa's subsidiary to construct the Fontana project, when required to obtain a license, indicates that not even the urgent demands of national defense can alter its apparent determination never willingly to submit any of its hydro projects to the duly enacted requirements of Federal law. . . .*
>
> Their attempted withdrawal is inconsistent with their contention regarding their interest in national defense and with their planned 25-year program of construction.
>
> *In our opinion Alcoa and the company have not dealt frankly in this matter, but have in the past undertaken and are now attempting to evade the plain provisions of the law.* (Emphasis added.)

Nantahala Power and Light Company, 2 F.P.C. 388, 390-91 (1941). An incidental effect of the subsequent conveyance to TVA of the Fontana site was the removal or elimination of the FPC's licensing authority over the Fontana project. *See* 16 U.S.C. § 831y-1. However, as is evident from the various agreements, the conveyance did not sever Alcoa's link with the project.

ment) to transfer the Fontana Dam site to TVA. The property so transferred was valued at approximately $3.5 million.[6] The transfer was effectuated by Alcoa's repurchase of the Fontana site from Nantahala for $1.9 million, or approximately $128 per acre. Nantahala had purchased the property from Tallassee at a cost of $112 per acre in 1929.

Under the terms of the OFA, the Fontana project, when completed by TVA, was to be operated together with other TVA generating plants owned by Alcoa's subsidiaries. The agreement refers to Alcoa as the "Company," and the "Company's plants" as including Nantahala's generating plants as well as the other plants now owned by Tapoco. The agreement called for the Alcoa system companies to convey the output from their generating plants to TVA in return for power and energy entitlements. The level and amount of power entitlements were dependent upon the level of generation which TVA controlled. In exchange for the companies' relinquishment of their control over stream flow and production from their plants (then operating or under construction) at Santeetlah, Cheoah, Calderwood, Nantahala and Glenville (Thorpe), TVA provided compensation power of 11,000 kw to the Alcoa system. Alcoa purchased Nantahala's portion of this compensation power for an annual payment of $89,200.

Although the OFA did not itself specify how the entitlements returned to the Alcoa system by TVA were to be divided among the system's member companies, the companies apparently would receive back as much or as little capacity and energy as each generated proportionately through its individually owned projects. In October 1954 Nantahala and Alcoa entered into a contract which called for Nantahala, when it had excess power, to make the excess available for Alcoa's use at its Tennessee facilities, and conversely, called for Alcoa to provide the power for Nantahala to meet its public load when Nantahala alone could not meet its public service obligation. *See Tapoco, Inc., Initial Decision*, 30 F.E.R.C. ¶ 63,050, at p. 65,273-74 (1985). Throughout the period of these contracts, Nantahala's capacity and energy production were far in excess of the demands of its then existing public service load. Nantahala's excess entitlements under OFA were then sold to Alcoa at "dump" prices. *See Utilities Commission v. Member-*

6. *Edmisten*, 299 N.C. at 435, 263 S.E. 2d at 586.

ship Corp., 260 N.C. 59, 131 S.E. 2d 865 (1963). There is no indication that the 1954 Alcoa-Nantahala contract was ever filed with the FPC as a tariff or rate schedule under Part II of the Federal Power Act. *See* 30 F.E.R.C. ¶ 63,050 at p. 65,275.

Moreover, when the OFA was signed in 1941, none of the Alcoa system plants subject to it had a license from the FPC under Part I of the Federal Power Act. The agreement itself was never filed with the FPC as a tariff or rate schedule during the twenty years that it remained in effect. As a consequence, the FPC never ruled upon the lawfulness or the agreement as a rate schedule while it was in effect. 30 F.E.R.C. ¶ 63,050 at p. 65,274.

In fact, it would appear from the contemporaneous decisions of the FPC that the federal agency only considered the operative terms of the OFA in an effort to determine whether it had licensing jurisdiction over three of the Alcoa system plants[7] which were subject to it—Calderwood, Santeetlah and Cheoah. At the time of the OFA's execution, Calderwood was owned by Alcoa subsidiary, the Knoxville Power Company (later Tapoco), and Santeetlah and Cheoah were owned by Alcoa subsidiary, the Carolina Aluminum Company. In 1941, the FPC instituted proceedings directing Alcoa and its subsidiaries to show cause why they should not be required to apply for licenses under Part I of the Federal Power Act for the continued operation and maintenance of the three plants. *In re Aluminum Co. of America*, 13 F.P.C. 14 (1954). Ultimate resolution of the matter was delayed by the pressures of the war emergency until March 1954. By that time, the respondent companies argued that the three plants were exempt from FPC jurisdiction because they were operated by TVA under the OFA.

The only actual discussion of the OFA comes in the FPC's discussion and rejection of the companies' arguments *in avoidance* of the agency's jurisdiction.

> *The Projects are Operated by Respondents.*—Under date of August 14, 1941, Alcoa and TVA entered into an agreement

7. All references in the opinion to "the Alcoa system" or the "Alcoa power system" or like phrases, refer exclusively to the subsidiary *operating* utilities which provide or provided the generation and transmission of electricity to their parent company Alcoa.

> (the Fontana Agreement) by the terms of which Alcoa transferred to the United States its interest, and those of its wholly-owned subsidiary, in the lands from the then proposed Fontana project and agreed upon a plan for "the coordinated operation of power facilities" of the Alcoa system and the TVA system. . . .
>
> The Fontana Agreement provides for the coordinated operation of power facilities of the two systems under the direction of TVA. Respondents contend that under this arrangement TVA "operates" the Calderwood, Cheoah, and Santeetlah projects within the meaning of the exemption provision of the last paragraph of Section 26(a) of the TVA Act (16 U.S.C. 831-Y-1). (Footnotes omitted.)

13 FPC at 21. The FPC went on to reject the exemption arguments advanced by Alcoa and its subsidiaries, finding that the Fontana Agreement "does not undertake to place the operation of Respondents' projects in TVA," but merely coordinates such operations as the companies themselves actually perform with the power facilities in the TVA system, "for the mutual benefit of Alcoa and TVA." *Id.* at 22. Consequently, the operating companies were ordered to file license applications under the Federal Power Act for the continued operation and maintenance of the three plants. *Id.* at 32. Thus, the OFA was not presented to the FPC by Alcoa and its subsidiaries for the purpose of affirmative regulation, but as part of an effort to preclude such federal oversight over the system's plants and power transactions.

During the period of the OFA's duration, a number of significant events occurred within the Alcoa system. As we have seen, in March 1954, thirteen years after the signing of the OFA, the FPC rejected the arguments of the Alcoa system and ruled that Cheoah and Santeetlah, among other plants subject to the OFA, required a license under the Federal Power Act. *In re Aluminum Company of America*, 13 F.P.C. 14.[8] In October of that year (1954),

8. Nantahala's hydroelectric generating plants subject to the various Fontana agreements were not required by the FPC to be licensed by that agency until the mid-1960's. *See Nantahala Power and Light Co.*, 36 F.P.C. 119 (1966), *rehearing denied*, 36 F.P.C. 581 (1966), *aff'd on review*, *Nantahala Power and Light Co. v. FPC*, 384 F. 2d 200 (4th Cir. 1967), *cert. denied*, 390 U.S. 945, 19 L.Ed. 2d 1134 (1968).

the wholly-owned subsidiary of Alcoa which was originally incorporated in Tennessee as the Knoxville Power Company, underwent a change of name to Tapoco, Inc. Within two weeks of its name change, Tapoco was domesticated as a North Carolina corporation.

As of October 1954, Tapoco owned two hydroelectric sites along the Little Tennessee River at Calderwood and Chilhowee in Tennessee. Tapoco, as well as acting as the power supplier to Alcoa's Tennessee aluminum smelting and fabricating facility, had at that time a public service load in Tennessee.

Another noteworthy event of October 1954 was the filing of a joint application by Tapoco and its affiliate, Carolina Aluminum Company to the FPC for a license to operate the "Tallassee project" along the Little Tennessee River in North Carolina and Tennessee. The project entailed the continued operation of the Cheoah and Santeetlah plants in North Carolina, and another existing plant in Tennessee at Calderwood (also subject to the OFA) and the construction of another hydroelectric generation plant at Chilhowee, Tennessee. The FPC's licensing order of March 1955 indicates that in their joint application, the companies stated that the energy from the Tallassee project, "is and will continue to be delivered to the Tennessee Valley Authority, which in turn delivers an equivalent amount of energy to the Aluminum Company of America at Alcoa, Tennessee, pursuant to the provisions of the Fontana agreement and the supplemental agreement thereto, dated August 14, 1941 and October 13, 1954, respectively." *Tapoco, Inc. and Carolina Aluminum Co.*, 14 FPC 610, 612 (1955). The licensing order continued by noting that the joint application states that after the exchange of energy between TVA and the Alcoa system pursuant to the Fontana agreement, "*[a]ll* the energy is used for aluminum production *except for* a small portion used for lighting in operators' villages." *Id.* at 612-13. (Emphasis added.) By June 1955, Tapoco had become the sole licensee of the four plants. *See Carolina Aluminum Co. and Tapoco, Inc.*, 14 F.P.C. 828 (1955); *Carolina Aluminum Co., Tapoco, Inc. & Nantahala Power and Light Co.*, 14 F.P.C. 829 (1955). Thereafter, Carolina Aluminum changed its name to its present name of Yadkin, Inc. The company now operates only the hydro facilities, not at issue here, which serve Alcoa's North Carolina, Badin works.

Conspicuous in its absence from the 1955 licensing order is any reference to the fact that TVA return power entitlements were also used to service Tapoco's public utility load in Tennessee and Nantahala's public utility load which, by the early 1950's, had increased to 10,000 customers, both residential and industrial, in a six-county area in North Carolina. *See Utilities Commission v. Mead Corp.*, 238 N.C. 451, 78 S.E. 2d 290 (1953). In addition, the licensing order fails to refer to the FPC's own earlier recognition that under the Fontana exchange and coordination agreements with TVA, Nantahala's larger plants were being operated together with Tapoco's plants as part of what the FPC termed " 'the coordinated operation of power facilities' of the Alcoa system and the TVA system." *In re Aluminum Company of America*, 13 F.P.C. at 21.

At about the same time that the federal license application was under consideration, Tapoco, Carolina Aluminum Company and Nantahala jointly filed for a certificate of public convenience and necessity with the North Carolina Utilities Commission in February 1955, to permit Tapoco to acquire, operate and control certain public utility properties belonging to Nantahala and Carolina Aluminum Company, including the Cheoah and Santeetlah plants and certain transmission lines. In the order granting the certificate, the Commission directed that Tapoco supply to Nantahala the power to satisfy Nantahala's public service load in the two villages of Santeetlah and Tapoco in Graham County. At that time, the two villages had a total population of about 300 people. This certificate is still in effect and Tapoco has never appeared before the Commission to abandon it, or have its terms modified. At the present time, the Village of Tapoco is still in existence and under the terms of the certificate and allocations made pursuant to the Fontana agreements, Tapoco still supplies power to Nantahala, which in turn serves the Village of Tapoco.

In the same month that Tapoco received its certificate of public convenience and necessity from the North Carolina Utilities Commission, it received from the State of Tennessee a certificate of public convenience and necessity to construct and operate the Chilhowee facility. Later in that year (1955), Tapoco contracted to sell its electric distribution system for the City of Alcoa, Tennessee to that municipality. The "City of Alcoa Resolution" which authorized the purchase indicates that the City

planned to look to TVA to supply it with the electric power previously supplied by Tapoco. Thus, Tapoco freed itself of its Tennessee public load and from that point onward, none of the power made available by TVA through the Fontana agreement had to be used to satisfy a Tennessee public load. As a result, Tapoco's share of the TVA return power could be devoted almost exclusively to Alcoa's aluminum production facilities. Notwithstanding the substantial generating capacity of Tapoco's facilities, which is three to four times as great as Nantahala's, Alcoa has historically needed to purchase additional power from TVA to supplement the combined output of its subsidiary power companies. To illustrate, during the test year 1975, Tapoco sold 1,365,499,000 kwh to Alcoa, yet, Alcoa purchased an additional 1,784,833,000 kwh from TVA.

During the period from 1950-1955, Nantahala expanded its facilities to provide additional power to Alcoa to enable it to meet the nation's increased aluminum needs during the Korean War. The major components of Nantahala's East Fork project, the Cedar Cliff, Bear Creek and Tennessee Creek dams and reservoirs were completed between 1952 and 1955. That year, 1955, marked the last year in which Nantahala added hydroelectric generating facilities subject to the coordination and exchange agreement with TVA. No additional generating capacity has been added to the Nantahala system whatsoever since 1957, despite clear indications that Nantahala's public service load was growing.

In this regard, we note that in 1941, Nantahala's public service load was only 25,984,275 kwh. By 1955, this load had increased to 115,735,461 kwh and by 1960, it stood at 172,451,768 kwh. *Utilities Commission v. Membership Corporation*, 260 N.C. 59, 66, 131 S.E. 2d 865, 870. During this same period, from 1941-1960, the relative volume of Nantahala's out-of-state sales to its parent Alcoa consistently outstripped its intrastate public service sales. For example, in 1943, approximately 95 percent of Nantahala's electric generation was sold to Alcoa (320,776,268 kwh), with its public service load receiving the remaining 5 percent (16,493,930 kwh). *Id.*

This imbalance of power consumption between Nantahala's parent and its public load, coupled with Nantahala's assigned role

in "the coordinated operation of power facilities of the Alcoa system and the TVA system,"[9] was observed to adversely affect Nantahala's intrastate rates as early as 1953. In an early Nantahala commercial rate case, *Utilities Commission v. Mead Corp.*, 238 N.C. 451, 78 S.E. 2d 290, Nantahala had sought to increase its rates to all industrial customers other than Alcoa, thus placing the burden of the increase upon the particular group of customers. The undisputed facts were to the effect that Nantahala had been selling more than 80% of its total generation of electric power to Alcoa at a price which was less than the cost of producing and distributing it. The evidence further showed that Nantahala derived the greater part of its revenue from customers other than Alcoa, who consumed only 18% of its power and who were charged approximately twice as much per kilowatt hour as Alcoa was charged. Additionally, it appeared the Nantahala had been earning a return of approximately 6.5% from the revenue collected from its non-Alcoa customers; whereas inclusion of the service and rate paid by Alcoa showed the company to be operating at a loss.

Nantahala sought to justify the differential in rates charged its parent and its public customers by asserting that the vast portion of its generation sold to Alcoa was "secondary" power, while its other commercial customers were supplied with "primary" or dependable power. The Commission approved the increase, finding no unlawful discrimination in this rate structure. On appeal to the Superior Court, the order of the Commission was reversed. This Court, in affirming the judgment of the Superior Court, stated that Alcoa was not entitled to a return on its investment in Nantahala in the form of a preferential rate to the extent it would work to the disadvantage of its subsidiary's other customers. 238 N.C. at 464, 78 S.E. 2d at 300. After noting that the question of "primary" and "secondary" power "was to a large extent the mere application of different labels to that which is essentially the same," *id.* at 465, 78 S.E. 2d at 300, the Court held that the actual differences in service and expense "were in no way comparable to the difference in rates which was so glaring as to compel the inference that it was unreasonable and therefore unlawful." *Id.*

9. *Cf. In re Aluminum Company of America*, 13 F.P.C. at 21.

Justice Barnhill, in a separate concurrence, commented upon one telling aspect of Nantahala's unique posture as a public utility whose largest customer was its parent-aluminum producer:

> Corporations must operate on a profit motive basis. Not so with petitioner. Financed as it is, it can afford—indeed it proposes—to operate at an apparent loss. By so doing it can evade the payment of its fair portion of State and Federal taxes.

238 N.C. at 467, 78 S.E. 2d at 301 (Barnhill, J., concurring).

Beginning in 1960, Alcoa and TVA began re-negotiation of the operational terms of the Original Fontana Agreement which were due to expire at the end of 1962. At the same time, Nantahala and Duke Power Company ("Duke") were engaged in separate negotiations to sell the assets constituting Nantahala's distribution system to Duke, with Nantahala retaining its major generating facilities and transmission lines. The sale would have enabled Nantahala to abandon its North Carolina public service load and to sell all of its generation (or the entitlements therefrom) to Alcoa, just as Tapoco had done. The 1961 Nantahala-Duke sale proposal received initial approval by both the North Carolina Utilities Commission and the Superior Court prior to the negotiation of the final provisions of the NFA in 1962. *See Utilities Commission v. Membership Corporation*, 260 N.C. 59, 131 S.E. 2d 865.

The New Fontana Agreement ("NFA"), dated 27 December 1962, modified and partially superseded the OFA. In essence, however, the NFA contained the same mechanics of power coordination and exchange as the original Fontana Agreement, except that the amount of power TVA was to make available to the Alcoa system under the NFA was fixed in advance by the agreement without regard to water conditions, rather than being calculated on the basis of amount actually generated by the Alcoa system's plants. As it did under the OFA, Alcoa again warranted that it was backing up or securing the performance of its subsidiaries in carrying out the coordination and exchange agreements with TVA.

In contrast to the OFA, which was negotiated and executed by Alcoa and TVA alone, Nantahala and Tapoco were signatory

parties to the NFA, although Nantahala was not a participant in the negotiations. Nantahala's failure to participate is not surprising in view of the Company's pending attempt to sell its distribution system to Duke, and so divest itself of its North Carolina public load. Later in 1963, this Court reversed the Commission's approval of the sale and ordered the case remanded for further consideration because the Commission had failed to make findings of fact with respect to essential aspects of the case and applied too lenient a standard for approval of abandonment of a public service franchise. *Utilities Commission v. Membership Corporation*, 260 N.C. at 68-69, 131 S.E. 2d at 871-72. The Court's discussion of Nantahala's stated reasons for abandoning its public load indicates the company's awareness that its generating capacity would be insufficient to meet its anticipated future requirements. In the wake of the decision, the attempt to sell Nantahala's distribution system to Duke was abandoned.

Under the NFA (still in effect during the test year 1975), TVA dispatched the operations of Tapoco's four plants and eight of Nantahala's largest plants, and received all of the electrical output of these plants. In return, the NFA provided that Nantahala and Tapoco together would receive an annual average of 218,300 kw, part of which was subject to some curtailment and interruption, to be divided between the companies as they saw fit.

The NFA also provided that it was to remain in effect for twenty years—until the end of December 1982. When the agreement took effect in January 1963 it was not on file with the FPC as a tariff or rate schedule and therefore was not examined at its inception for its lawfulness. *See* 30 F.E.R.C. ¶ 63,050 at 65,276. It was not until 1966 that the NFA was filed with the FPC as a tariff or rate schedule under Part II of the Federal Power Act, in response to that agency's request that the companies do so. Both Tapoco and Nantahala (concurring in Tapoco's filing) stated that the filing was "under protest"—that is, undertaken subject to the right to contest the FPC's authority to regulate the operations under the NFA. Moreover, its terms were not formally scrutinized by the federal authorities until after three of Nantahala's wholesale customers filed a complaint raising the matter in 1978. *See Nantahala Power and Light Co. v. FERC*, 727 F. 2d 1342 (4th Cir. 1984).

The NFA, like the OFA, failed to specify how the power made available to the Alcoa system by TVA was to be divided among the members of the system. On the same day that the NFA became effective, 1 January 1963, Alcoa and Nantahala entered into a subordinate allocation agreement establishing Nantahala's share of the return power entitlements.

The 1963 Alcoa-Nantahala Apportionment Agreement provided that Nantahala was to receive, as its share of NFA entitlements each month, a variable of the larger of one-twelfth of its annual primary energy capability of 360 million kwh or its actual generation. A 1960 Ebasco Study, undertaken for Nantahala by independent experts, had established the average annual generation of Nantahala's plants subject to the NFA at 424 million kwh annually. Thus, under the 1963 Agreement, Nantahala was guaranteed its primary generation and was to benefit from additional generation. Moreover, the agreement provided that Alcoa was to pay Nantahala the sum of $89,200 annually as compensation for allowing TVA to operate Nantahala's projects. Significantly, the 1963 Agreement fixed no capacity or demand limitation upon Nantahala's use of the energy returned. However, unlike the 1954 Alcoa-Nantahala contract which was subordinate to the OFA, the 1963 contract did not impose an obligation upon Alcoa to satisfy any deficiency when Nantahala did not have sufficient power to meet its public load. It appears that the 1963 allocation agreement was never filed with the FPC. *See* 30 F.E.R.C. ¶ 63,050 at p. 65,277; *Nantahala Power and Light Co., Initial Decision*, 15 F.E.R.C. ¶ 63,014, at p. 65,035 (1981).

Between 1963 and 1971 the North Carolina public load, although growing, still remained below Nantahala's primary generation and Nantahala did not need all of its entitlements of 360 million kwh; Alcoa utilized the remainder under its separate agreement with Nantahala. However, by 1971, Nantahala's public load had grown to the point where the utility no longer had excess energy under the NFA to sell to its parent Alcoa. Moreover, by 1971, Nantahala recognized the need to obtain a supplemental source of power to meet the anticipated needs of its public service load in North Carolina. TVA, to whom Nantahala was already interconnected, was chosen as the source of this supplemental power; however, TVA required a formal agreement between Nantahala and Tapoco apportioning their NFA entitlements before it

would negotiate a supplemental power contract with Nantahala. Accordingly, in 1971 Alcoa conducted an apportionment study to measure the energy and capacity contributions of Nantahala and Tapoco. Pursuant to the study made by Alcoa's power consultant, George Popovich, Nantahala executed an apportionment agreement with Tapoco and then entered into an additional purchase contract with TVA.

The 1971 Nantahala-Tapoco Apportionment Agreement (the "1971 Apportionment Agreement") called for Nantahala to fix a limitation on its share of energy from TVA at 360 million kwh annually (*i.e.*, only its primary energy capability). Tapoco was to receive the remainder of the power made available by TVA under the NFA. The 1971 Agreement contained no provision for Nantahala to receive the $89,200 previously provided for under the 1963 Alcoa-Nantahala allocation agreement in compensation for Nantahala allowing TVA to control its facilities.

Simultaneously with the execution of this 1971 Apportionment Agreement, Nantahala entered into a contract with TVA to purchase additional power from that agency. By this agreement, in addition to paying TVA's charge for all energy consumed in excess of 360 million kwh per year, Nantahala was required to pay a charge for the demand of its system above 54,300 kw at any instant. This latter figure represents the capacity limitation assigned to Nantahala under the 1971 Apportionment Agreement with Tapoco.

The 1971 Apportionment Agreement was not filed with the FPC as a tariff or rate schedule for almost ten years, until 1980. *See* 30 F.E.R.C. ¶ 65,030 at p. 65,277; 15 F.E.R.C. ¶ 63,014 at p. 65,035. As had been true of the NFA itself, at the time the agreement became operational, and for the bulk of its life, its terms were not scrutinized by the federal authorities for their lawfulness.[10]

10. We find it noteworthy, as did the Administrative Law Judge in the most recent Nantahala case before the F.E.R.C., that 1982 marked the first time in the forty years since the Alcoa-TVA coordination and exchange agreements had begun, that the Alcoa system had given notice to the F.E.R.C. that it was planning to terminate one of these agreements as well as a separate contract between members of the system and seeking approval in advance for the new agreements which were to supersede the expiring contracts. 30 F.E.R.C. ¶ 63,050, at p. 65,280.

Since the inception of the 1971 Apportionment Agreement, Nantahala has not had available to it for sale, through its portion of return power entitlements, enough electricity to meet its North Carolina public service load. During the 1975 test year, Nantahala generated about 560 million kwh. Despite the fact that its public service load was only slightly in excess of 450 million kwh, Nantahala was constrained to purchase an additional 81,265,370 kwh of electricity from TVA at a cost of $1,500,000, due to the allocational limitations of the NFA and 1971 Apportionment Agreement. 1971 also marked the final year in which Alcoa purchased power from Nantahala, looking instead to Tapoco and TVA to fulfill its energy requirements.

The intervenor's evidence shows that subsequent to that time, Nantahala could have used on its system all of the capabilities it contributed to the TVA system under the NFA and failed to receive back in entitlements of comparable worth. The quantity of power Nantahala purchases from TVA is determined by the magnitude of the shortfall resulting when the hour-by-hour load on the Nantahala system exceeds the level of TVA return entitlements set under the NFA and apportioned to Nantahala under the 1971 Apportionment Agreement. Since 1971, when the annual level of Nantahala's load first exceeded its entitlements, the purchased power costs have become a major operating expense for Nantahala.[11] Thus, Nantahala's contractual arrangements with its affiliates and TVA have dramatically influenced Nantahala's costs in providing service to its public load.

C.

There is apparently no dispute between the parties as to the Commission's authority to implement a roll-in of Nantahala's and Tapoco's properties and financial data for rate making purposes without regard to the separate corporate entities of these utilities, once it has properly determined that these corporate affiliates in fact constitute a single, unified "utility enterprise" or system. The propriety of the separation or rolling-in of properties

11. The "fuel" for Nantahala's hydroelectric generating units is water with no fuel cost. The fuel used by TVA to produce the power it sells to Nantahala is a mix of relatively costly nuclear and fossil fuel. TVA's generation mix contains only a modest increment of hydroelectric generation.

of affiliated corporations for rate making purposes, being merely a step in the determination of costs properly allocable to the various classes of service rendered by a utility, is widely recognized as dependent upon the particular characteristics of the system or systems in question, and upon the facts and circumstances of each case. *See, e.g., Colorado Interstate Gas Co. v. FPC*, 324 U.S. 581, 89 L.Ed. 1206 (1944); *Central Kansas Power Co. v. State Corporation Commission*, 221 Kan. 505, 561 P. 2d 779 (1977); *Georgia Power Co.*, 52 F.P.C. 1343 (1974). *See generally*, Annot., 16 A.L.R. 4th 454 (1982).

Moreover, as FERC itself has expressly recognized, "the question of whether to treat various entities as an integrated system for rate making purposes is not a purely factual question, but also rests on criteria which each rate making authority may deem relevant." *Nantahala Power and Light Co., Opinion No. 139-A*, 20 F.E.R.C. ¶ 61,430, p. 61,869 (1982). Accordingly, in the parallel FERC wholesale rate case in which Nantahala's wholesale customers advocated the implementation of a roll-in, FERC, while adverting to the fact that the North Carolina Utilities Commission had, "based on a similar record, reached a different conclusion concerning rolled-in costing," *id.*, declined to order a roll-in for determining Nantahala's wholesale costs of service. The Fourth Circuit Court of Appeals, in affirming FERC's determination, stated that "[a] decision to order roll-in is essentially a matter of Commission discretion" which would not be overturned on appeal where supported by substantial evidence. *Nantahala Power and Light Co. v. FERC*, 727 F. 2d 1342, 1346 (1984).

[1] Therefore, it is clear that the North Carolina Utilities Commission has the authority, in the first instance, to determine for itself the relevant criteria to apply to the factual question of whether to treat Nantahala and Tapoco as an integrated system for rate making purposes and its determination will not be disturbed on appeal where supported by substantial evidence. The companies do not contend that the Commission decision is unsupported by substantial evidence; they merely argue that the Commission *ignored* evidence[12] tending to show that Nantahala and Tapoco are separate electric utility companies.

12. We will address this point more fully in Part II, D *infra*.

The Commission's decision of whether to implement a roll-in is based upon a factual predicate consisting of three basic propositions: (1) Tapoco is a North Carolina public utility, subject to the Commission's rate making authority; (2) Nantahala's and Tapoco's hydroelectric facilities constitute a unified, single system, operating under conditions rendering a roll-in appropriate; and (3) Alcoa is a statutory North Carolina public utility, subject to the imposition of a refund obligation in the exercise of the Commission's general rate making jurisdiction. In the record before us, we find plenary evidence in support of the Commission's determination that Nantahala and Tapoco constitute a single, integrated electric system and should be treated as such for the purposes of calculating Nantahala's retail rate base and costs of service.

Upon remand, the Commission held a separate *de novo* hearing on the question of its jurisdiction with respect to Tapoco and Alcoa. Based upon the testimony and exhibits presented at the *de novo* hearing and matters judicially noticed, the Commission, in an order entered 3 October 1980, found and concluded that both Tapoco and Alcoa were subject to its regulatory authority under Chapter 62 of the North Carolina General Statutes.

1.

[2] With respect to Tapoco, the Commission made certain findings of fact regarding its development and acquisition of hydroelectric facilities clothed with public service obligations in North Carolina, most notably, the facilities at Santeetlah and Cheoah. Specifically, the Commission found that Tapoco is a domesticated North Carolina corporation organized to produce and sell electricity; that Tapoco's articles of incorporation provide that one of its purposes is to provide power to the public and those articles authorize Tapoco to exercise the power of eminent domain; that Tapoco has a North Carolina certificate of convenience and necessity to operate the Cheoah and Santeetlah facilities, obtained when it purchased these facilities and certain transmission lines (owned by Nantahala) from its public utility affiliates, Carolina Aluminum Company and Nantahala; that this certificate is subject to the condition that Tapoco provide Nantahala with the power needed to serve the Villages of Tapoco and Santeetlah; that Tapoco's certificate of convenience and necessity

is still active, Tapoco never having petitioned to have its certificate abandoned; that Tapoco has the responsibility to make available a tap point on its station service transformer at the Cheoah power house for Nantahala's use in providing electricity for serving its customers in the Village of Tapoco; and that Nantahala is presently providing service to the Village of Tapoco and charging its customers there for the electricity provided on the basis of rates approved by the Commission. The Commission also made findings with respect to the electricity Tapoco delivers to TVA and Alcoa by virtue of the various intra- and intercorporate agreements discussed above.

The Commission then based its conclusion that Tapoco is a public utility in North Carolina and subject to its jurisdiction on three grounds:

1. It is a public utility within the meaning of G.S. § 62-3 (23)a.[13]

2. It is a public utility for rate-making purposes within the meaning of G.S. 62-3(23)b.[14]

3. It is a public utility by virtue of having obtained a certificate of public convenience and necessity some twenty-

13. N.C.G.S. § 62-3(23)a provides in pertinent part as follows:

(23) a. "Public utility" means a person, whether organized under the laws of this State or under the laws of any other state or country, now or hereafter owning or operating in this State equipment or facilities for:

1. Producing, generating, transmitting, delivering or furnishing electricity, piped gas, steam or any other like agency for the production of light, heat or power to or for the public for compensation; . . . .

14. N.C.G.S. 62-3(23)b provides:

(23) b. The term "public utility" shall for rate making purposes include any person producing, generating or furnishing any of the foregoing services to another person for distribution to or for the public for compensation.

N.C.G.S. 62-3(21) provides:

"Person" means a corporation, individual, partnership, company, association, or any combination of individuals or organizations doing business as a unit, and includes any trustee, receiver, assignees, lessee, or personal representative thereof.

five years ago, and having operated under that certificate since that time.[15]

Although Tapoco assigned error to the Commission's finding that it is a North Carolina public utility and argued in its brief to the Court of Appeals that the portions of the Commission's order which declare Tapoco to be a "public utility" under North Carolina law should be vacated and reversed, in its new brief to this Court, Tapoco does not challenge the Court of Appeals' affirmation of the Commission's determination that Tapoco is a statutory public utility. Rather, Tapoco presents a single and somewhat confused argument that the Commission "abused its regulatory authority by asserting jurisdiction over Tapoco when it did not and could not regulate Tapoco's rates and service."

Tapoco first argues to this Court, as it did to the Court of Appeals, that the Commission could not "divert" power from the Tennessee industrial load (Alcoa) served by Tapoco's four hydroelectric projects because these projects were licensed by FERC in 1955 to serve that load *exclusively* and the Commission is without authority to impose a state law limitation on the terms and conditions of Tapoco's federal license. Tapoco relies on *First Iowa Hydro-Electric Cooperative v. FPC*, 328 U.S. 152, 90 L.Ed. 1143, *reh'g denied*, 328 U.S. 879, 90 L.Ed. 1647 (1946) and *Town of Springfield v. Vermont Environmental Board*, 521 F. Supp. 243 (D. Vt. 1981) to support its "diversion" argument.

15. N.C.G.S. 62-110 provides:

No public utility shall hereafter begin the construction or operation of any public utility plant or system or acquire ownership or control thereof, either directly or indirectly, without first obtaining from the Commission a certificate that public convenience and necessity requires, or will require, such construction, acquisition, or operation: Provided, that this section shall not apply to construction into territory contiguous to that already occupied and not receiving similar service from another public utility, nor to construction in the ordinary conduct of business.

In *Utilities Commission v. Telegraph Co.*, 267 N.C. 257, 148 S.E. 2d 100 (1966), we observed that it would be both arbitrary and in excess of the statutory authority of the Commission to grant a certificate of public convenience and necessity to conduct a business which is not a public utility. None of the respondent companies contends that the Commission acted in excess of its statutory authority in granting Tapoco its certificate of convenience and necessity in 1955.

The other portion of Tapoco's argument to this Court, however, was not presented to either the Commission or the Court of Appeals and was not made the basis of Tapoco's assignments of error. That argument, presented now for the first time in this appeal, is that Tapoco has been "misjoined" and should be dismissed as a party to this proceeding because the Commission *did not* grant relief with regard to Tapoco's rates in the Sub 29 (Remanded) proceeding. Accordingly, Tapoco now contends that it was "misjoined" as a party respondent and that under Rule 21 of the North Carolina Rules of Civil Procedure it should be "dismissed forthwith from the instant proceeding," and be awarded the costs of this appeal.

[3] We first note that pursuant to Rule 16(a) of the North Carolina Rules of Appellate Procedure, the scope of our review from a unanimous decision of the Court of Appeals is limited to consideration of the questions properly presented in the new briefs required by Rule 14(d)(1) and 15(g)(2) to be filed in this Court. Rule 16(a) further provides that a party who was an appellant in the Court of Appeals, and is either an appellant or an appellee in the Supreme Court, may present in his brief any question which he has properly presented for review to the Court of Appeals. However, questions properly presented for review in the Court of Appeals but *not* presented and discussed in the new briefs to this Court are deemed abandoned under Rule 28(a). Therefore, Tapoco is deemed to have abandoned and waived further review of the question of its public utility status under North Carolina Law.[16]

A corollary to the rule that this Court's scope of review is limited to questions properly presented to the Court of Appeals is the rule that a party may not present for the first time in its brief to this Court, a question raising issues of law not set out in the assignments of error contained in the record on appeal. App. R. 10. Consequently, the question of "misjoinder" under Rule 21 of the Rules of Civil Procedure, appearing as it has for the first time in Tapoco's new brief filed in this Court, has not been prop-

16. We have, however, under Rule 2 of the Rules of Appellate Procedure, reviewed the Commission's findings and conclusions in the course of our review of the questions properly preserved, find them to be supported by substantial evidence and affirm the Commission's determination as to Tapoco's public utility status on each of the three grounds specified in its orders entered in the Sub 29 (Remanded) proceedings.

erly presented for review and we need not address it in the course of our discussion.

[4] The only questions that Tapoco has correctly preserved for further review are, therefore, whether the Commission is preempted from implementing a roll-in methodology for setting Nantahala's retail rates by virtue of the fact that Tapoco's four hydroelectric plants are under federal license and whether the Commission's order places an indirect burden on interstate commerce by diverting the economic benefits of Tapoco's inexpensive hydroelectric power from its Tennessee industrial customer, Alcoa, to Nantahala's North Carolina public service customers. Inasmuch as Tapoco has merely joined in the brief of Alcoa on the latter point, we will discuss the Commerce Clause issues adverted to by Tapoco in the section of this opinion addressing Alcoa's constitutional argument. With respect to Tapoco's licensing argument, we have little trouble in concluding that the Commission's order has in no way contravened the terms and conditions of Tapoco's federal license.

Under Part I of the Federal Power Act, 16 U.S.C. §§ 791a-823a, the Federal Power Commission (and now the FERC) has exclusive jurisdiction to license the construction and operation of hydroelectric projects on navigable rivers within the United States, and to fix the terms and conditions of any such license. Tapoco's argument that the issuance of its 1955 federal license to construct and operate the four plants of the "Tallassee Project" preempts the Commission from implementing a roll-in is based upon Tapoco's assertion that the plants were licensed by the FPC for "the express purpose of supplying power to Alcoa's Tennessee Operations." We find nothing in the licensing order to indicate that the FPC intended to reserve all of the hydroelectric production from (or economic benefit of) the four Tapoco dams for Alcoa's exclusive use. In its brief, Tapoco places great reliance upon the underscored language contained in a portion of the 1955 licensing order:

> [T]he energy being developed by the constructed developments of the project and the energy to be developed by the proposed development is and will continue to be delivered to the Tennessee Valley Authority, which in turn delivers an equivalent amount of energy to the Aluminum Company of

> America at Alcoa, Tennessee. . . . All the energy is used for aluminum production except for a small portion used for lighting in operators' villages. . . .
>
> * * *

[T]he project is best adapted to a comprehensive plan for the improvement and utilization of waterpower development, and for other beneficial public uses, including recreational purposes.

Deleted from the quoted portion of the licensing order, however, is the revealing opening phrase: "According to the joint application. . . ." It is therefore obvious that the language relied upon by Tapoco, rather than constituting an edict by the FPC that all of the energy produced by the developments comprising the "Tallassee Project," now solely owned by Tapoco, be dedicated to the permanent and exclusive use of Alcoa's private industrial operations, merely contains a restatement by the FPC of the assertions made by Tapoco and Carolina Aluminum Company in their joint licensing application. The order itself contains no express or implied directive from the FPC that the energy produced by these hydro projects be reserved for the sole and exclusive use of Alcoa in its Tennessee aluminum plants, either in the section containing FPC's findings of fact or in its decretal paragraphs.

Moreover, 16 U.S.C. § 802(b) requires that, prior to the issuance of a hydroelectric license, a licensee must submit evidence of compliance with state law "with respect to the right to engage in the business of developing, transmitting, and distributing power. . . ." *Cf.* N.C.G.S. § 62-3(23)a(1). At the time of application, on 25 October 1954, Carolina Aluminum was a North Carolina public utility carrying a public service load in this state and Tapoco was a Tennessee public utility carrying a public service load in that state. On 23 February 1955, before the license was granted by the FPC, Tapoco, which had earlier domesticated in North Carolina, was issued a certificate of convenience and necessity by the North Carolina Utilities Commission to own and operate the Santeetlah and Cheoah facilities. That certificate expressly noted that Tapoco had an obligation to serve the public with electric energy from the projects. When the federal license was issued, it also noted that Tapoco had an obligation to serve the public with electric energy from the projects.

In the 1955 licensing order, the FPC found as a fact that Tapoco and Carolina Aluminum each had submitted satisfactory evidence of compliance with the requirements of all applicable laws for its respective State insofar as necessary to effect the purposes of a joint license for the project, to the extent of the ownership and operation of the project by each applicant. The evidence submitted by joint applicant Carolina Aluminum included its compliance with North Carolina requirements. When, shortly thereafter, the FPC authorized transfer of Cheoah and Santeetlah from Carolina Aluminum and to Tapoco only, it noted that Tapoco had "submitted evidence of compliance with the requirements of all applicable state laws of Tennessee and North Carolina. . . ." 14 F.P.C. at 828.

On the basis of the foregoing, in its final order filed 28 January 1982 the Commission concluded, and we agree, that "[t]o the extent that the federal licenses for Tapoco's dams speak toward dedication of the electric energy, such dedication would of necessity include the using and consuming public of North Carolina." We therefore reject Tapoco's argument as to the preemptive effect of the federal license on the Commission's authority to implement a roll-in methodology in determining Nantahala's retail rates.[17] In any event, as will be discussed *infra*, the roll-in itself does not effectuate a diversion of Tapoco's actual energy production to the North Carolina public load; it merely accomplishes for bookkeeping purposes what is an accomplished fact in the organization and operation of the two companies: the allocation of the combined costs of production for the unified Nantahala-Tapoco system as between the jurisdictional North Carolina retail public load and the nonjurisdictional Alcoa industrial load.

17. We note in passing that the Administrative Law Judge presiding over the latest Nantahala wholesale rate case came to the identical conclusion regarding the intent and effect of the 1955 PFC licensing order. 30 F.E.R.C. ¶ 63,050, at p. 65,290-91. After observing that the FPC had apparently been given insufficient information about the features and consequences of the Alcoa system's coordination and exchange agreements with TVA, and the fact that Nantahala's steadily increasing public load was also serviced under the Original Fontana Agreement, the ALJ concluded that under these circumstances, "with the licensing order silent on such critical points, there is no reasonable basis to conclude that the Commission [FPC] intended to reserve for Alcoa's use alone all of the Tapoco power." *Id.* at 65,291.

2.

[5] The Commission also made findings of fact, amply supported by the evidence of record, as to the existence of a single, unified hydroelectric generating and transmission system consisting of the combined facilities of Nantahala and Tapoco and wholly owned by Alcoa. The evidence in support of these findings may be summarized as follows:

Nantahala and Tapoco are both wholly owned subsidiaries of a single corporate parent, Alcoa. Nearly all of the facilities of Nantahala and Tapoco are situated on the Little Tennessee River and its tributaries. The two power companies are located in contiguous areas in western North Carolina, with portions of Tapoco's physical plant intruding into Nantahala's service area. The Nantahala and Tapoco electric facilities are physically interconnected with each other, with one generation and one distribution connection at Tapoco's Santeetlah facility; power can be dispatched and transmitted from the facilities of one to the facilities of the other. Standing between the two companies' Little Tennessee generation sites is the Fontana project; Nantahala's hydro developments are all located upstream of the Fontana dam, while Tapoco's are all downstream, thus poised to receive the downstream benefits of the Fontana project. Nantahala's eleven developments are smaller and relatively more expensive than Tapoco's four larger developments. The combined resources of the two provide relatively low-cost power and energy under the coordination and exchange agreements with TVA.

The Original and New Fontana Agreements treat the facilities of Nantahala and Tapoco without discrimination and make them an integrated part of, and subject them as a unit to coordination by TVA. By the terms of these agreements, TVA receives the output of all of the hydro resources of both Nantahala and Tapoco, except for three small plants of Nantahala. In addition, the agreements call for Tapoco and Nantahala to turn over to TVA control of production and stream flow. Accordingly, TVA determines for Tapoco and Nantahala, as a single entity, both electric generation and stream flow and operates them as an integrated system and a coordinate part of TVA's own system. In turn, Tapoco and Nantahala jointly receive back from TVA certain entitlements of power which they divide between themselves

by the 1971 Apportionment Agreement. Coordination was regarded as an efficient and economical method to maximize production of electricity from the various plants and to enhance the overall reliability of the pool of power available to the combined system. It is evident from the terms of the Fontana agreements that Alcoa and TVA intended the Fontana project, once it was completed, to be operated together with other TVA generating plants in coordination with certain plants of the combined Nantahala-Tapoco system.

The intervenors' expert engineering witness, David A. Springs, testified at the remanded hearings that it is a "false and arbitrary assumption that NP&L [Nantahala] and Tapoco operate as isolated systems when in fact they do not." When witness Springs was asked whether the Nantahala and Tapoco facilities should be operated as a separate and independent system, he replied: "No, by coordinating them as one with TVA, the outputs of the generating resources are maximized." Springs added that, from an engineering standpoint, the Nantahala and Tapoco facilities should be operated as one utility. With regard to the question of whether Nantahala was designed to operate as part of an integrated system as opposed to operating as a stand-alone company, Springs stated, "NP&L could not have been designed the way it was to ever operate as an isolated system."

Not only was Nantahala designed to operate as an integral part of a larger utility enterprise, but its projects were developed and put into service in accordance with Alcoa's aluminum production needs rather than scheduled in accordance with the size of its public load. The greater portion of Nantahala's capacity, the Glenville (Thorpe) and Nantahala projects, were added in the early 1940's before there was a significant public load in need of their output. Conversely, since the mid-1950's no significant capacity has been added to the Nantahala system, despite clear signs that its public load would place increasingly greater demands upon its facilities. This pattern of development reflects the increased electric power demands of Alcoa on the combined system during the Second World War and Korean War, and its generally decreased and levelized demand in the post-war period.

Springs also testified to the propriety of using a roll-in methodology in determining the appropriate rate base and allocation of

cost responsibility for the customers served by Nantahala's facilities. Springs' conclusion, adopted by the Commission, that a roll-in is mandated in the case of Nantahala and Tapoco, is based upon his analysis of actual company cost responsibilities under the current and historical operating and contractual conditions tying the Nantahala and Tapoco facilities into a single, unified electric system. As Springs explained, cost-of-service rate making is simply a function of rationally assigning to various classes of customers cost responsibility for the facilities available for and used in their service. In cases where facilities are jointly used by two or more groups of customers under circumstances where, for example, a stand-alone method of costing fails to identify appropriate customer loads or where actual customer cost responsibility is distorted by unreasonable power pool agreements a roll-in methodology is appropriate for rate making purposes.[18]

In the case of Nantahala, Springs testified that actual customer cost responsibility for the facilities available for that service cannot be accurately computed on the basis of the percentage of return power entitlements it receives from TVA separate and apart from the total pool of power available to Nantahala and Tapoco as a combined system, because these entitlements reflect neither the generating facilities actually available for Nantahala's retail service, nor the actual use of those generating facilities by those customers. As the intervenors' witness explained:

> A cost-of-service study, whether it be rolled-in or single company, is simply a means of assigning to customer groups the appropriate cost responsibility for the demands the customers place upon the resources of the utility . . . a rolled-in cost-of-service approach [is appropriate] for NP&L and Tapoco, because it is impossible to separate out the functional relationship between the generating resources operated by these companies and the load they each serve.
>
> In a normal utility operation, the ownership of generating resources by particular operating companies reflects the identification of resources to customer loads. In the normal course of development, a utility company will develop the resources in the geographic area, which the customers

18. *See, e.g., Georgia Power Co.*, 52 F.P.C. 1343.

would look to in order to serve their loads. Usually, companies will integrate their resources into a combined system, such as the Southern Company system, and experts might legitimately disagree as to whether it is more appropriate to measure customer demands for service on an individual company basis or a system-wide basis. This is because system-wide needs and the needs of customers of individual companies both impact [sic] the development, planning and operation of power supply resources. *However, in the case of NP&L and Tapoco, I find no significant pattern of power supply development, planning or operation on any basis other than a combined basis.* (Emphasis added.)

In short, it is apparent that the evidence of record overwhelmingly supports the Commission's finding and conclusion that "the Nantahala and Tapoco electric facilities constitute a single, integrated electric system and are operated as such by, and as a coordinated part of, the TVA system," and its further conclusion that, "for purposes of setting Nantahala's rates in this proceeding, the Nantahala and Tapoco systems should be treated as one entity with respect to all matters affecting the determination of Nantahala's reasonable cost of service applicable to its North Carolina retail operations."

3.

[6] Finally, with respect to Alcoa's status as a North Carolina public utility, the Commission correctly noted that despite the fact that Alcoa would not be a statutory public utility under the definitions contained in N.C.G.S. § 62-3(23)a and (23)b, it is a public utility under the definition contained in N.C.G.S. § 62-3(23)c, which provides:

> The term "public utility" shall include all persons affiliated through stock ownership with a public utility doing business in this State as parent corporation or subsidiary corporation as defined in G.S. 55-2 to such an extent that the Commission shall find that such affiliation has an effect on the rates or service of such public utility.

N.C.G.S. § 55-2(9), in turn, provides as follows:

> "Parent corporation" means a corporation which is a dominant shareholder, as herein defined. A corporation through

> which, by virtue of its shareholdings alone, a parent corporation has power to exercise the control which makes the latter a parent corporation is itself a parent corporation. A parent corporation with respect to which another corporation is a parent corporation is a "subsidiary corporation."

Finally, N.C.G.S. § 55-2(6) states:

> "Dominant shareholder" means a shareholder of a particular corporation, domestic or foreign, who by virtue of his shareholdings has legal power, either directly or indirectly or through another corporation or series of other corporations, domestic or foreign, to elect a majority of the directors of the said particular corporation.

Applying these statutory definitions to the respondent corporations, the Commission concluded that (1) Alcoa, as the owner of all of the outstanding stock of Nantahala, a North Carolina public utility as defined by N.C.G.S. § 62-3(23)a, is a parent corporation of Nantahala within the meaning of N.C.G.S. § 62-3(23)c, and is itself a public utility under that section, and (2) that Alcoa's affiliation with Nantahala has had an effect on Nantahala's rates, as evidenced by the terms and results of the New Fontana and 1971 Apportionment Agreements.

We have reviewed the record with regard to these matters and find that the evidence fully supports the Commission's determination that Alcoa is a North Carolina public utility under N.C.G.S. § 62-3(23)c, by virtue of the effect Alcoa's "affiliation" with Nantahala has had upon Nantahala's rates. The historical and current operating conditions tying Tapoco and Nantahala together clearly show that Nantahala is part of a single utility enterprise, created by Alcoa as part of a plan to secure for itself, through the separate corporate entities of its public utility subsidiaries, the large quantities of low-cost power it requires for its aluminum smelting and fabricating operations. Alcoa's unified development of the Little Tennessee River through its subsidiary power companies resulted in the assigning of the system's least expensive utility resources to its exclusive service, through Tapoco, while relegating the relatively expensive portion of those resources to the system's public service load through Nantahala. This development, in turn, has had an enormous impact on the rates Nantahala charged to its retail customers.

Indeed, nearly every major document charting Nantahala's development contains self-referential language describing Nantahala and (later) Tapoco's projects as parts of "the Alcoa power system," that is, the Alcoa power generating and distribution system. For example, in its 1940 application to the Department of War for a national defense certificate of necessity to build its largest hydroelectric facilities, Nantahala stated that the justification for its intended developments at Glenville (Thorpe), Nantahala and Fontana were the enormous electric needs of Alcoa. The application described "the system" which these developments were to be added to as follows:

> At the present time, Alcoa receives power from three dams located on tributary waters of the Tennessee River at Calderwood, Tennessee, and Tapoco, North Carolina (Cheoah and Santeetlah developments). . . .
>
> . . . The new developments will be upstream from the present developments. It is contemplated that they will store water during winter months, and will be used in the dry season to produce additional power and also to make available additional water for the developments downstream. The estimated total addition to *the Alcoa power system* is 51,500 k.w., part of which will be produced at the new developments and part from additional water released for use downstream.
>
> The Glenville project will have installed generating capacity of 21,500 k.w. and will add 17,500 k.w. to *the system*. This power will be used as soon as available for the Alcoa pot line scheduled for January 1941.
>
> The Nantahala project will have installed generating capacity of 42,200 k.w. and will add an estimated 34,000 k.w. *to the system*. It will be completed about August, 1942 and will thereafter supply power for one of two Alcoa pot lines planned for January, 1942. (Emphasis added.)

Similarly, both the Original and New Fontana Agreements, by which Alcoa caused its subsidiaries' hydroelectric facilities to be coordinated in operation with the TVA system, contain references to Alcoa as the "Company" and to the "Company plants" as facilities owned by Nantahala and Tapoco. Article III of the New Fontana Agreement, entitled "Operation of Company's Hydroelectric System," states in part:

> 1. Definitions
>
> For purposes of this agreement, "Company's plants" or "Company's hydroelectric plants" shall mean the following hydroelectric generating plants (and associated diversion dams) which are owned by Nantahala and Tapoco.
>
> * * *
>
> [There follows a list of eight of Nantahala's plants and four of Tapoco's plants.]
>
> The words "transmission facilities of Company," "Company's transmission facilities," and words of similar import shall mean the transmission facilities of Tapoco [and] Nantahala. . . .

In like manner, Article II of the New Fontana Agreement describes the division of rights, benefits and obligations under that contract in terms of a single, integrated system, with Alcoa ultimately guaranteeing the performance of all obligations of the system members thereunder.

> Wherever this agreement provides an obligation or right on the part of Company to generate, sell, or transmit electric power and energy or an obligation or right on the part of Company to own or operate facilities for the generation, sale or transmission of electric power or energy, such obligation or right shall be performed and discharged or enjoyed as the case may be by Nantahala or Tapoco. However, Alcoa warrants and represents to TVA that it will secure the performance of all of the obligations of Company under this agreement.

Of course, Alcoa's involvement in the development, design and operation of the hydroelectric resources of Nantahala and Tapoco is by no means limited to the role of guarantor described above. Perhaps the most succinct and telling account of this role and its purpose is found in the historical study of "the Alcoa story," published in 1952, and entitled *Alcoa: An American Enterprise*. The book, written by Charles C. Carr, who was for many years Director of Public Relations for the company, is a self-professed objective account of Alcoa's history as gleaned from

Alcoa records and files.[19] In the chapter concerning "Water Power," the author explained that in the aluminum business, which requires vast amounts of electricity to produce the metal, electricity is a commodity; an essential part of the cost of every pound of metal along with labor, raw materials, capital investment and the wearing out of equipment.

As early as 1893, Alcoa selected water power as the one source of cheap electric energy best suited to aluminum production. Actuated by the search for low-cost hydroelectric power from its earliest days, Alcoa formed a number of water and power companies in various parts of this country and Canada. When these proved insufficient for Alcoa's growing needs, "Alcoa looked elsewhere for power and located it, about 1909, in the mountains of Tennessee-North Carolina." Carr, *Alcoa: An American Enterprise*, at 93. As Carr observed, "[t]he story of Alcoa's power projects in North Carolina would make a chapter by itself." *Id.* at 95.

> Spurred on by necessity, Mr. Davis and his associates started to acquire riparian properties along the Little Tennessee River and its tributaries in 1910. Studies and plans that contemplated the *unified development of the entire river and its tributaries above Chilhowee, Tennessee, were undertaken.* The assurance of adequate power from that swift-flowing mountain river and its tributaries, *to be developed as needed,* gave Mr. Davis the vision of what is today this country's largest aluminum plant, at Alcoa, Tennessee. On March 6, 1914, the first pot lines of an aluminum reduction works started operating at this location.
>
> The Tallassee Power Company in North Carolina was acquired in 1914 and operated under that name until 1931 when it was changed to the Carolina Aluminum Company. *The Nantahala Power & Light Company was organized as a public utility on July 23, 1929, to develop as needed the power sites which had been owned by the Carolina Aluminum Company*

19. *See* Carr, *Alcoa: An American Enterprise*, "A Note of Explanation," at v-vi (1952). Aluminum Company of America holds the copyright to this publication in its name and portions of the book relevant to this discussion are included as an exhibit in the record before the Commission and on appeal. The intervenors' witness David A. Springs refers to the book in his testimony and the Commission referred to the book in its order.

> *on the upper reaches of the Little Tennessee and its tributaries, the Nantahala and Tuckasegee Rivers.*
>
> *The Nantahala Power & Light Company, a wholly-owned Alcoa subsidiary, is essentially a utility company serving many western North Carolina communities with electricity* to light their homes and to run their motors for commercial, farm and household use. *Its long time President was the late J.E.S. Thorpe, an Alcoa veteran of thirty years' service and well-known utility operator in the Southeast. Mr. Thorpe, who had served as head of Nantahala Power & Light Company for twenty-one years at the time of his death in 1950, was recently honored in a lasting manner by the Directors of Alcoa. The name of a mountain power development, originally known as the Glenville project, was changed to the Thorpe Development.*
>
> *Although its first duty is to serve the communities in its territories, Nantahala Power & Light Company has in its domain such large hydro projects as Glenville and Nantahala, which augment the supply of power in the North Carolina mountains available for aluminum-making.*
>
> * * *
>
> Harnessing the swift-flowing Little Tennessee and its tributaries in their rush through the Great Smokey Mountains is a saga in which many Alcoa veterans have played a part. . . . (Emphasis added.)

Id. at 93-95.

Finally the author discusses what he considers to be the unusual degree of cooperation achieved between "Government" (TVA) and "private industry" (Alcoa) in developing the "fountainhead of the power projects on the Little Tennessee," the Fontana project. According to Carr, Alcoa had purchased nearly all the necessary land in the Fontana basin for development purposes, had found it necessary to become a purchaser of TVA power to supplement its own sources and then, in 1941, "to the surprise of many people who could see 'no good in TVA,' *Alcoa gave to the Governmental authority, without monetary fee, its site at Fontana, where most of the necessary land had been acquired, parcel by parcel, over many years." Id.* at 97. With this

grant, went roadway relocations and engineering data Alcoa had assembled for the construction of the great dam and power project at the Fontana, North Carolina site.

> In return, TVA agreed to build Fontana, the great storage reservoir which would regulate the flow of water at Alcoa's hydro projects and Cheoah and Calderwood, as well as at TVA's downstream projects. Alcoa was influenced in its decision by the Water Power Act of 1920 [predecessor to the Federal Power Act], which would have required the Company to obtain from the Federal Power Commission a license to build Fontana. This license would have given the Government the right to "recapture" the project after fifty years.
>
> *A second part of the Fontana agreement gave TVA the right to control the impounding and release of water to all of Alcoa's hydroelectric developments on the Little Tennessee and to use this generating capacity as an integral part of the TVA power system. In return for this, Alcoa received from TVA approximately the number of kilowatt hours generated at Alcoa plants during a calendar year, and in addition 11,000 KW of primary power without cost. The first part of the Alcoa-TVA agreement, wherein the Fontana project regulates the flow of water at Cheoah and Calderwood, is in perpetuity. The second part, recited in this paragraph, can be cancelled by either party on three years' notice after January 1, 1952.*
>
> * * *
>
> *This agreement made possible the integrated operation of the water powers of Alcoa and TVA, including the Fontana project.* Its result was the maximum production of electric energy from the available water power, not only on the Little Tennessee River but also throughout the entire Tennessee Valley, which is served by the great Tennessee River and all its tributaries. (Emphasis added.)

Id. at 97-99.

Although Nantahala and Tapoco were operating under the New Fontana Agreement and the 1971 Apportionment Agreement during the test year relevant to this proceeding, these agreements were negotiated in the context of the prior Fontana

and apportionment agreements and the operating conditions established thereby. As we have seen, under the OFA, Alcoa (Tapoco) received the benefit of downstream storage derived from TVA's construction of the Fontana project, with no further capital investment by Alcoa. TVA released *in perpetuity* its right to claim downstream benefits against Alcoa in exchange for the transfer of title to the Fontana site. Alcoa caused Nantahala, a public utility with the power of eminent domain, to transfer its title to the Fontana site and its rights to develop that project to TVA, despite the fact that Nantahala was not permitted to be a signatory party of the OFA. Nantahala was not positioned to receive any portion of the downstream storage benefits because it owns no facilities downstream of the Fontana Dam, while Tapoco, and through it Alcoa, was positioned to receive all the downstream benefits because all of Tapoco's projects are downstream of the Fontana site. In addition, Alcoa gave up to TVA a large portion of the dependable capacity from the hydro projects owned by Nantahala and Tapoco.

The New Fontana Agreement, essentially an amendment to the OFA, was signed at the end of 1962, after approximately two years of negotiations between TVA and Alcoa. The 1962 Agreement essentially expanded the coordination of the two systems by fixing the availability of capacity and energy returned from TVA without regard to stream flow conditions. However, in the bargain, dependable hydro capacity was traded away in exchange for improvements in the availability of energy for aluminum production. This produced a significant increase in the degree of availability of secondary energy to Alcoa. This energy, subject to prolonged periods of interruption, is unsuited to the needs of a public load, which requires peaking capacity to meet fluctuating customer demands. As it had done with the OFA, Alcoa, now through its employee George Popovich, represented its own interests and those of Tapoco and Nantahala in the negotiations with TVA over the NFA's terms and conditions. Nantahala itself had no direct participation in the negotiations. Significantly, the Alcoa negotiation paper, entitled "NOTES ON MEETING WITH TVA —MARCH 2, 1962," refers to the pending transfer case and rate case then before the Commission as the "Nantahala problems."

It is evident that prior to this Court's action in *Utilities Commission v. Membership Corp.*, 260 N.C. 59, 131 S.E. 2d 865, Alcoa

personnel had believed that the sale to Duke was to be approved. Thus, an Alcoa memorandum entitled "*RE: FONTANA AGREEMENT*" dated 23 August 1960, concludes as follows:

> *One final note, the entire TVA proposal is based upon the sale of the Nantahala Power Company.* TVA proposed that if the sale was not complete at the time this new proposed contract becomes effective, they would increase the power available to us under the purchase contract to whatever amount is necessary for us to handle the Nantahala loads. . . . This would be done on a temporary basis and would be reduced concurrent with the transfer of the Nantahala properties to Duke. (Emphasis added.)

The final Alcoa memorandum after completion of all negotiations for the NFA, dated 6 November 1962, reflects the continuing intention on the part of Alcoa to accomplish the transfer of Nantahala's distribution system and public service load to Duke. However, no revisions were thereafter made to the NFA or to the purchase and apportionment agreements subordinate to it to take into account the growing public load serviced by Nantahala. In addition, the Commission found that the NFA's structure rendered it necessary for Nantahala to enter into the subordinate 1963 Apportionment Agreement with Alcoa, five days after the signing of the NFA, in order to secure Nantahala's participation in the TVA return entitlements. This was done by means of a monetary supplement from Alcoa to Nantahala and a guarantee of a certain share of power entitlements from the TVA return.

The Commission concluded that the foregoing evidence clearly demonstrates that the NFA was tailored to meet Alcoa's aluminum production needs without consideration of Nantahala's public service needs and that this arrangement had a considerable impact on Nantahala's rates.

By the time the 1971 Apportionment Agreement was signed, the interconnected power supply structure had long been in place, and Nantahala found itself without sufficient power to service its public load, which had been growing at an annual rate of approximately 8.5 percent. Having added no additional generating capacity, since 1957, and having failed to enter into other power supply contracts tailored to its public load requirements, Nantahala found itself in the position of having to make supplemental pur-

chases of power from TVA and passing those additional costs along to its public customers in the form of increased rates.

Again, it was an Alcoa employee, George Popovich, who conducted the 1971 apportionment study and devised the apportionment formula that was incorporated into the 1971 Agreement between Tapoco and Nantahala. Moreover, during the course of the negotiations "between" Nantahala and Tapoco over the division of return power entitlements, Popovich apparently represented the interests of *both* Nantahala and Tapoco at the "bargaining table." When questioned as to his role, Popovich conceded that he wore "both their hats" during these negotiations adding merely that in view of Nantahala's public utility responsibilities, "I think my Nantahala hat was bigger than my Tapoco hat." At this point, we note only that in its examination of the results of these contractual arrangements upon Nantahala's retail costs of service, the Commission came to precisely the opposite conclusion.

The net effect of Alcoa's "affiliation" with Nantahala is evidenced by a pattern of operation of Nantahala's power supply resources under the various Fontana and apportionment agreements largely inconsistent with and ultimately detrimental to, its ability to render service at just and reasonable rates to its retail customers. Further, as the Commission itself concluded, "Nantahala was not designed as, and is not in reality, a separate utility system but, rather, is a part of an integrated Alcoa system with Tapoco."

Moreover, Alcoa's involvement in the development of Nantahala's and Tapoco's North Carolina hydro resources does not stop with these contractual arrangements. Rather, as this Court noted in *Edmisten,* Alcoa's role also extends to "the ultimate operating and accounting policies of both utilities. The chief executive officers of both Nantahala and Tapoco report directly to an Alcoa vice president. Members of the board of directors of both utilities are employees of Alcoa." 299 N.C. at 435, 263 S.E. 2d at 586. Indeed, Nantahala's president, William M. Jontz, had his original employment conversations with Alcoa officials in Pittsburgh, Pennsylvania. Although his employment as president of

Nantahala began on 1 June 1976, he did not meet with the Nantahala Board of Directors until the latter part of July 1976.[20]

Similarly, the president of Tapoco is a direct employee of Alcoa serving in the dual status of power manager of Alcoa's Tennessee operations and president of the utility company. His sole office is located at Alcoa's south main plant at Alcoa, Tennessee. Furthermore, Alcoa owns 100 percent of the capital stock of Nantahala and Tapoco. The assistant controller of Alcoa, Robert D. Buchanan, testified that he has the "general responsibility for the financial accounting for Alcoa and its subsidiaries, and as such ha[s] responsibility for the books and records and financial policies of Tapoco and Nantahala."

The foregoing evidence manifestly demonstrates the substantial and detrimental impact Alcoa's "affiliation" has had upon Nantahala's rates and service to its North Carolina public utility customers, and fully supports the Commission's conclusion that Alcoa is a North Carolina public utility under the provisions of N.C.G.S. § 62-3(23)c.

In summary, the evidence of record gathered at the remanded hearings before the Commission in this general rate case establishes beyond question three basic propositions: (1) Tapoco is a North Carolina public utility; (2) the hydroelectric facilities of Nantahala and Tapoco constitute a unified, single system, operating under conditions rendering a roll-in rate making methodology appropriate; and (3) Alcoa is a statutory North Carolina public utility to the extent that its affiliation with Nantahala has affected Nantahala's rates.

20. Significantly, Nantahala's employment contract with its president describes the "major general objectives" of such employment to include both the company's management *and* the development of plans "for the possible sale or other disposition" of Nantahala, said goals to be accomplished "so that there is little or no adverse impact on the operations and assets of Nantahala's parent company [Alcoa] and its subsidiaries in North Carolina, including, but not limited to, . . . Tapoco, Inc. and Yadkin, Inc. . . ." Under the section governing base salary, the contract provides for achievement awards based upon the president's performance with respect to these objectives, "To be determined annually by the three-member [Alcoa] group among the Board of Directors of Nantahala. . . ." Finally, under provisions entitled "Nondisclosure," the president is not to engage in any act which would, *inter alia*, tend to prejudice the business of "Nantahala *or* of Nantahala's parent company [Alcoa] and its subsidiaries . . . Tapoco, Inc. and Yadkin, Inc.

D.

The Commission, after finding that Nantahala and Tapoco are a single, integrated electric system, joined the assets, properties, plants and working capital requirements of both companies into a unified rate base, totaled joint revenues and operating expenses, and assigned the combined system the rate of return approved for Nantahala alone in the 1977 proceedings. From these elements, a combined system revenue requirement was derived. These aspects of the Commission's order are not challenged by the companies. However, the controversy between the intervenors and the companies over the proper cost allocation methodology to be used in apportioning the combined revenues, expenses and investment of the unified system between the retail customers in North Carolina and the non-jurisdictional Alcoa industrial load in Tennessee lies at the heart of this appeal.

Generally speaking, the allocation methodology proposed by the companies through their expert witness Herbert J. Vander Veen assigns customer cost by utilizing the entitlements of the New Fontana Agreement and the 1971 Apportionment Agreement; whereas the allocation methodology proposed by the intervenors through their expert witness David Springs, and adopted by the Commission, is grounded upon the assignment of cost responsibility to the public load and to Alcoa on the basis of which load actually used the capability available from the generating facilities of the combined system. The jurisdictional allocation factors utilized by the Commission are generally accepted factors commonly employed by the Commission in setting intrastate retail rates for other public utilities serving in more than one jurisdiction. The unique problem posed by this case lies in the fact that Nantahala's available power supply was contractually reshaped by the quantity and design of the entitlements returned by TVA under the NFA and allocated to Nantahala under the 1971 Apportionment Agreement. In effect, the companies treated Nantahala as part of a unified system when dealing with Nantahala's contribution to the pool of power turned over to TVA and with respect to TVA's dispatch of Nantahala's facilities, but not when determining Nantahala's share of the entitlements returned to the Alcoa system. Thus, Nantahala's share was computed *as if* Nantahala were a stand-alone company. In the process, Nantahala

received little or no value in return for certain contributions it made to the integrated system.

The Commission, in rejecting the companies' proposed allocation methodology, reasoned that it would be unjust to Nantahala's retail rate payers to allocate demand and energy related costs on the basis of TVA return entitlements because the terms of the NFA had been structured to meet Alcoa's industrial needs and not Nantahala's public service needs. Moreover, the combination of the NFA and the 1971 Apportionment Agreement forced Nantahala to purchase costly additional power irrespective of its production capacity. The companies argue that the Commission was constrained by the doctrine of federal preemption to utilize the NFA demand and energy entitlements in determining Nantahala's demand and energy related costs because the NFA and 1971 Apportionment Agreement are FERC-filed wholesale rate schedules, the reasonableness of which may not be reinvestigated by state public service commissions, and the economic results of which must be accepted in setting retail rates. Additionally, they argue that the manner in which the Commission allocated the rolled-in costs places an impermissible burden upon interstate commerce by affording North Carolina customers a "first call" on both the energy output of the combined system and the economic benefits of Tapoco's lower-cost production. A proper understanding of our conclusion in Part II, A and B, *infra*, that the Commission is neither preempted by the Federal Power Act and Supremacy Clause, nor forbidden by the Commerce Clause of the United States Constitution from implementing the rolled-in rate making methodology developed in this case necessitates a brief review of the Commission's findings with respect to the power supply agreements at issue.

Initially, it must be pointed out that the Commission's discussion of the NFA and 1971 Apportionment Agreement occurred in the context of addressing the impropriety of basing *cost allocations* on demand and energy entitlements as contained therein. The Commission was not concerned with the reasonableness of the power exchange agreements and associated system costs *per se*, but with the question of which load should be held responsible for which portion of these costs in its rates. Put another way, it is evident that the Commission's in-depth examination of the terms of these contracts was undertaken as part of its process in choosing between the competing jurisdictional cost allocation methodologies presented by the parties and not in an effort to either reform the contracts or to alter the actual flow of return power thereunder.

In some twenty pages of its rate reduction order, the Commission exposed and "fleshed out" the extensive network of detriments and inequities to Nantahala and its customers embedded in the terms of the NFA and 1971 Apportionment Agreement. In essence, the Commission found that a disproportionate amount of the capacity and energy resources of the combined Nantahala-Tapoco system, perfectly usable by the load characteristics of the Nantahala public load, were traded away to reform the TVA return entitlements to fit the needs and characteristics of an aluminum smelting and fabrication operation. Because Nantahala is structured, operated and treated as an integral unit of the combined system, rather than as a stand-alone company, the detriments it incurs under the integrated system's power supply contracts result in concealed benefits flowing to Tapoco, and ultimately to its parent and customer, Alcoa. While "costs" charged to the combined system under these contracts might be considered objectively fair and reasonable from the wholesale perspective, the public customers of Nantahala were found to have fared badly when that utility was artificially separated out of the unified system for allocation purposes, and then forced to bear the added responsibility for costs of purchased power from TVA.

The Commission found a number of specific inequities in terms of cost responsibility to Nantahala and concealed benefits to Alcoa arising out of both the NFA and 1971 Apportionment Agreement, and divided its treatment of these agreements into separate discussions. Another portion of the order analyzes the manner in which the companies employed the data contained in the agreements in developing their cost allocation methodology. Finally, the order discusses the mechanics of the allocation adopted by the Commission from the proposal of the intervenors and utilized in fixing Nantahala's rates. We will use the subject headings corresponding to those portions of the order in our summary of the discussion contained therein.

Concealed Benefits of the Apportionment Agreement

(1) Quantity of Nantahala's Production.

In 1962, Alcoa power consultant George Popovich determined that under the NFA, Nantahala should be apportioned annual energy entitlements guaranteed at minimum, to return to Nantahala an amount equivalent to its primary energy capability of 360 million kwh plus its actual production in excess of that amount, which was 79 million kwh of average energy; 66 million kwh when Nantahala's non-Fontana generation is taken out. Popovich's 1962 figures were derived from an independent engineering study made by Ebasco in 1960 for Nantahala, and accepted by Alcoa as the basis for Nantahala's entitlements under the 1963 Alcoa-Nantahala Apportionment Agreement. By that agreement, Nantahala received annually an average of 426 million kwh, of which 360 million kwh was guaranteed as a minimum. The 426 million kwh of return power was approximately the same amount as Nantahala contributed to TVA under the NFA. Yet despite these facts, when Popovich devised the 1971 Apportionment Agreement, Nantahala received only 360 million kwh annually. Thus, Nantahala was deprived of an average of 66 million kwh annually. The Commission concluded that this detriment to Nantahala constitutes a benefit to Tapoco that is passed on to Alcoa.

(2) Quantity of Nantahala's Peaking Capacity.

The 1960 Ebasco Study computed Nantahala's plant capacity, under the most adverse water conditions, at 85,400 kw. After deducting the three small plants excluded from the NFA, that capacity is 84,300 kw. Alcoa's acceptance of these computations is reflected in a number of internal documents cited by the Commission in its order. As was true of the energy entitlements, this study formed the basis of Nantahala's capacity entitlements in the 1963 Alcoa-Nantahala Agreement. Under it, Nantahala was permitted to use capacity without a pre-set limitation. Therefore, Nantahala was able to use actual capacity to the limits assigned by the 1960 Ebasco Study in meeting its customer demands. However, when Popovich conducted his study for the 1971 Apportionment Agreement, while accepting the most adverse water (*dependable*) capacity factor of 84,300 kw, he deducted 27,500 kw for the "largest unit out" to reach an *assured* capacity of 54,300

kw. This deduction is for the Nantahala facility which forms upwards of 50 per cent of the entire Nantahala generation system of 11 dams. Thus, under the 1971 Apportionment Agreement, Nantahala was assigned a peaking capacity of 54,300 kw. The result of this limitation is that any time Nantahala has to provide a customer demand in excess of 54,300 kw, it must pay a monthly demand charge to TVA for all power over that limitation. If the limitation were set at Nantahala's capacity level determined by the "loss of load probability" method, the monthly demand charge would be only the amount between 81,800 kw and the excess customer demand over and above that amount. The Commission concluded that demand costs thereby imposed on Nantahala for use of capacity between its assigned capacity of 54,300 kw and its assured capacity of 81,800 kw, would represent an expense to Nantahala and thus a savings to "its New Fontana Agreement sister, Tapoco," since the capacity constraints for the TVA return entitlements are jointly shared by them under the NFA.

The difference in amount between the capacity assigned to Nantahala under the 1971 Apportionment Agreement and what the Commission has determined its assured capacity to be results from the different methodologies employed by the companies and the intervenors in determining Nantahala's assured capacity. The intervenors' witness Springs testified that the proper reserve margin for Nantahala should be the margin used by TVA, which is "the loss of load probability" method. Use of this method would recognize that Nantahala is operated as part of the coordinated Alcoa-TVA system rather than as a stand-alone utility, and would result in a reserve requirement of about 3 per cent. Using a 3 per cent reserve in place of the "largest unit out" reserve, which, in this case is upwards of 50 per cent, would establish a capacity under the most adverse water conditions of 81,800 kw as opposed to Popovich's calculation of 54,300 kw.

The Commission concluded that significant cost is shifted to Nantahala by the unfair and unwarranted limitation of its capacity to 54,300 kw; conversely, that expense, in the form of demand charges paid to TVA, is a concealed benefit to Alcoa. The basis for the Commission's conclusion that the capacity limitation assigned to Nantahala under the 1971 Apportionment Agreement was unwarranted lies in the Commission's rejection of the "larg-

est unit out" adjustment to actual capacity for reserves in computing Nantahala's assured capacity. The order states as follows:

> *If* Nantahala were a separate and independent system, a deduction of the "largest unit out" might be appropriate to determine assured capacity. *However, Nantahala is not and never has been a separate electric system—it was not so designed.* Nantahala's two largest facilities are Thorpe (previously Glenville), . . . and Nantahala, ... The Thorpe and Nantahala facilities comprise about 65% of Nantahala's entire system. At the time of their construction, *Alcoa obtained a certificate of necessity from the War Department and expressly argued and avowed that they were part of the Alcoa system. . . .*
>
> *Furthermore, for the past 40 years, both Nantahala and Tapoco have been operated as an integral part of the TVA electric system pursuant to the provisions of the Fontana and New Fontana Agreements. Moreover, when Alcoa negotiated these agreements with TVA, it did not bargain for return power from TVA as if Nantahala was an independent power system but rather the attributes of the Alcoa system were melded together, with the TVA system for evaluation purposes. . . .*
>
> *With Nantahala and Tapoco being thus integrated into and coordinated with the TVA system, it is not appropriate to determine Nantahala's assured capacity by configuring Nantahala as a single independent and isolated system and to use the "largest unit out" methodology.* Instead, Nantahala should be treated as part of the TVA system and the reserve margin used by TVA should be applied. TVA does not use a reserve of "largest unit out" but rather uses "the loss of load probability method." (Emphasis added.)

(3) Nantahala's Upstream Benefits.

Nantahala's projects are upstream of Tapoco's projects, with the exception of Santeetlah. As a consequence, water that is stored by Nantahala can be released to flow downstream and be used by Tapoco for production of electricity. Therefore, Nantahala's storage has a value to Tapoco which is undiminished by the fact that TVA's Fontana Project now lies between Nantahala

and Tapoco. A 1956 TVA study estimated the upstream storage benefits of the two major Nantahala projects to be a continuous relative contribution of 4,300 kw to Tapoco's downstream Calderwood and Cheoah projects. This is an equivalent of 37,668,000 kwh annually as an upstream benefit from Nantahala to Tapoco. However, under the 1971 Apportionment Agreement, Nantahala received no credit for this benefit to Tapoco, which was in turn passed on to Alcoa.

(4) Nantahala's Entitlement for Operating Its Properties in Accordance with the Fontana Agreement.

By the 1941 Fontana Agreement, Nantahala, at the instance of Alcoa, gave to TVA the right, *in perpetuity*, to control the storage and flow of water from its several hydroelectric projects. The Commission found that Nantahala's giving up of rights unquestionably constituted a loss of considerable value for which Nantahala was entitled to compensation. With the 1963 Alcoa-Nantahala Apportionment Agreement, Alcoa agreed to continue to pay to Nantahala monies for Nantahala's loss of those operational rights. Moreover, the agreement clearly showed that TVA was continuing to pay value for those rights, which value is reflected in the TVA return entitlement of the New Fontana Agreement. This fact was also reflected in the Commission's own earlier findings with respect to the TVA return entitlement in the year 1963 in Docket No. E-13, Sub 13. Yet despite the fact that the NFA includes in the TVA return entitlement a reimbursement by TVA for the right to operate Nantahala's projects, for which Alcoa previously paid $89,200 annually to Nantahala, no credit was given to Nantahala for that entitlement under the 1971 Apportionment Agreement. In other words, Nantahala receives neither an energy credit nor a monetary payment for the right given up. The Commission concluded that since the TVA payment for the operational rights, which is paid with energy in the NFA rate entitlement, did not go to Nantahala, it inured to the benefit of Tapoco, which, in turn passed this benefit to Alcoa.

(5) Nantahala's Value to the TVA Interconnected System.

The Commission found that another failure of the 1971 Apportionment Agreement regarding Nantahala's participation is that the Popovich apportionment formula does not consider the

proper value to TVA of the fact that Nantahala, Tapoco and the TVA systems are interconnected.

> Interconnection is of considerable value to TVA completely aside from the fact that Nantahala's rate base includes in it certain assets devoted to the interconnection, which assets are entitled to earn a rate of return. Because Nantahala is not an isolated system, it should be receiving the usual benefits that accrue from coordinated operation. Yet, Nantahala does not receive the usual benefits of an interconnected and coordinated system.

Relying on Alcoa documents reflecting the path of its negotiations with TVA over the New Fontana Agreement, the Commission found that the integrated systems factor was recognized by Alcoa to be of great value to TVA, a recognition that Alcoa was able to capitalize on later in arriving at the final terms of the agreement. As indicated, some of the values of integration are the need for smaller reserves and the fact that TVA actually controls production of generation and storage waters. However, one of the larger benefits is the value in integration of Nantahala's projects that are upstream of TVA's Fontana Project. The Commission noted that in an integrated system such value is maximized; Nantahala's projects contributed upstream benefits not only to Tapoco's downstream projects, but also to TVA's downstream Fontana Project. In fact, the entire TVA Tennessee River system receives the benefit of the storage of all of these projects located on the Little Tennessee River. This is especially so given TVA's control of all of the Nantahala and Tapoco reservoirs under the terms of the Fontana Agreement. Based upon the results of a TVA study of combined downstream storage benefits, the Commission determined that Nantahala's annual upstream benefit to TVA is 70,956,000 kwh.

However, when the NFA bargain was struck, the TVA and the Alcoa systems agreed to cancel out their respective upstream benefits. The Commission observed that since Nantahala provided benefits upstream to both Tapoco and TVA, and TVA provided benefits upstream to Tapoco, it was Tapoco that gained by the mutual cancellation, to the detriment to Nantahala of the value of 70,956,000 kwh annually. The Commission further concluded that Nantahala should have received back an equivalent amount of

energy under the 1971 Apportionment Agreement from Tapoco. Because Nantahala received no such benefit under the Popovich apportionment formula, the Commission concluded that to Tapoco's benefit, Nantahala was deprived of one value of the interconnection with the TVA system. This concealed benefit flowing from Nantahala to Tapoco, is of course, passed on by Tapoco to Alcoa.

In summarizing its discussion of the detriments to Nantahala from the 1971 Apportionment Agreement, the Commission totalled the annual kilowatt hours which Nantahala contributed in average production to the system and for which no credit was received in return and determined that Nantahala was deprived of a total value of 200,224,000 kwh annually. In addition to which, Nantahala received no credit for its peaking capacity over the 54,300 kw which was assigned to it, as a result of which Nantahala must pay additional demand charges to TVA when monthly demand exceeds assigned capacity. After quoting a portion of this court's opinion in *Edmisten* regarding the terms of the 1971 Apportionment Agreement, the Commission concluded:

> Now that considerably more of the various detriments to Nantahala have been exposed and fleshed out, it is apparent that the 1971 Apportionment Agreement works an extensive injustice on Nantahala and its public rate payers, the gravity of which far exceeds even that envisioned by the Supreme Court.

Concealed Benefits of the New Fontana Agreement

The Commission found the concealed benefits flowing from Nantahala to Alcoa by virtue of the NFA to be entirely different in nature from those which flow from Nantahala to Tapoco, and ultimately to Alcoa from the 1971 Apportionment Agreement. The basic inequity to Nantahala arising out of the NFA is that the energy entitlement returned to Nantahala and Tapoco from TVA is structured to meet Alcoa's demand for a certain amount of stable electricity for purposes of aluminum production rather than a demand for a public load. Consequently, the NFA returns to the system an average of 218,300 kw of energy at a high load factor with minimal peaking deviation, which is principally designed to service Alcoa's pot-lines and other production electrical

requirements. Even the interruptible and curtailable energy entitlement returned to Nantahala-Tapoco is in increments of wattage that conform to the demands of a pot-line so that, if power is interrupted or curtailed, Alcoa can respond by cutting out a particular pot-line.

Nantahala, on the other hand, has a fluctuating demand for energy which has peaks and valleys. Its electrical requirement is for assured, but constantly variable amounts of energy. Nantahala needs peaking capacity and its generation projects possess peaking capacity, yet the NFA traded away that peaking capacity to TVA. The Commission agreed with the intervenors that the trade-off of Nantahala's own peaking capacity, at a time when Nantahala's load required such peaking capacity, thus forcing the utility to purchase capacity back at a higher price from TVA, was not the result of "enlightened, arm's-length bargaining" and that the detriment resulting to Nantahala from the design of the NFA entitlements flows to Alcoa as a benefit.

In fact, the intervenors' evidence demonstrated that Alcoa reaped enormous benefits through the trade in the improvement of the availability of Tapoco's secondary energy production *from* a level of 42 per cent average curtailment *to* an average curtailment rate of only 8 per cent. In addition, Tapoco's generation statistics reflect the benefits of coordination with the Fontana Project and other forms of integration with TVA. These figures are inconsistent with the isolated system model utilized as a basis for the 1971 Apportionment Study. Again, it was evident that the two operating subsidiaries were treated as a single system for purposes of bargaining with TVA over the value of their combined contribution to the TVA system, and were only separated out as if they were independent systems for the purposes of dividing the return entitlements between them.

The Commission noted that "Alcoa was in direct control of the [NFA] negotiations, and, unlike the Nantahala ratepayers, has had every ability to protect its own interests during the negotiations. Respondents cannot now be heard to claim that they are dissatisfied with the NFA so as to place the cost responsibility for the deficiencies of that agreement upon Nantahala's ratepayers." In explanation of the design of the NFA, the Commission observed that during the negotiation stage of the NFA, the parties contemplated the sale of Nantahala's distribution system to Duke. The sale would have left Nantahala with its generation, but without a public service load, so that all of its NFA entitlements would be satisfactory for delivery to Alcoa irrespective of quantity and design; in no manner was the NFA structured to meet Nantahala's public service needs.

Next, in passing, the Commission rejected the remedy of regulatory reformation of the NFA to properly award to Nantahala its just entitlements as, of necessity, somewhat hypothetical at this stage of the case. Rather, for cost allocation purposes, the Commission concluded that the "roll-in technique avoids the need for complete identification of inequities and is nicely suited as a proper alternative to reformation of contracts." On the basis of its discussion of the various "detriments" to Nantahala resulting in "benefits" to Alcoa, both directly and through Tapoco, and "upon careful consideration of the entire evidence of record," the Commission concluded that it should reject the companies' proposed allocation methodology in that "said methodology in all material respects is based upon the New Fontana Agreement and the Tapoco-Nantahala Apportionment Agreement." Under a separate heading, the Commission discussed the manner in which the companies employed the data contained in the NFA and the Apportionment Agreement in greater detail to show why their allocation methodology was not proper for computing Nantahala's retail costs of service.

The Mathematics of Allocation

In this portion of the order, the Commission described the competing allocation methodologies presented by the companies and the intervenors for determining Nantahala's demand and energy costs. In general, the method proposed by the companies' witness Vander Veen derived the demand and energy charges from the demand and energy entitlements allocated to Nantahala under the NFA and 1971 Apportionment Agreement.

Vander Veen's Nantahala-Tapoco roll-in cost of service study differs fundamentally from the study submitted by the intervenors' witness Springs in that Vander Veen includes the *entire* Alcoa load served by Tapoco *and* TVA for purposes of computing the Nantahala-Tapoco system's demand allocation factor. In other words, Vander Veen adjusted Tapoco's 1975 book figures to re-

flect a non-utility, 235 Mw direct power purchase by Alcoa from TVA pursuant to a separate, non-Fontana Alcoa-TVA purchase contract as if it were part of the Nantahala-Tapoco system's *generating* resources. With this non-utility addition to the system's power supply, Vander Veen performed a demand allocation which assumed that the system peak occurred at the hour of the Nantahala system peak in 1975, and that at that hour Tapoco had available to serve the Alcoa load both Tapoco's NFA entitlements and the full amount of the Alcoa purchase contract (as adjusted) of 235 Mw.

In addition, for demand cost allocation purposes, Vander Veen's method recognizes the distinction between firm and nonfirm NFA entitlements. He used only the firm power available under the NFA to meet system demand, thus removing entirely the amount of capacity that can be curtailed and interrupted from the capacity available to serve system load. As the Commission found, the upshot of this technique is to render 90 Mw of actual return entitlements *valueless* for meeting the system demand at any time, whether or not power is actually curtailed, and even when there may be additional make-up demand. Another 1/16th (*i.e.*, 15 Mw) of the 90 Mw interruptible power returned by TVA under the NFA was also taken out of Tapoco's demand allocation, so that a total of 105 Mw was removed for both the curtailable and interruptible power, and rendered valueless for cost allocation purposes. The effect on Nantahala's costs of Vander Veen's technique is to dramatically increase Nantahala's proportionate share of the demand charges even though both Nantahala and Tapoco take under the NFA and Tapoco takes three times as much power as Nantahala.

In contrast to the foregoing cost of service analysis, the intervenors' evidence showed, and the Commission accepted, that the non-utility direct industrial purchases that Alcoa makes from TVA are not properly considered a *utility* function of either Tapoco, Nantahala or the combined utility system of both and so are not properly includable in the cost of service allocation. Furthermore, the demand credit Vander Veen assigns to Alcoa because of the interruption and curtailment features of the NFA is not supported by the actual features of the unified system. The Commission adopted the view taken by the intervenors' witness

Springs that use of only firm power available to meet system demand distorts rather than reflects customer cost responsibility.

> Although it is not unusual for an industrial customer to receive a credit for accepting interruptible power, the rationale for this is that the utility providing the service to that customer will save the cost of carrying reserves. The ability of a utility to provide such credits is limited by its need for reserves. There should be no credit for interruptions which do not result in cost savings to the supplying utility. Mr. Vander Veen's demand credit unfairly assigns to other customers the fixed costs necessary to generate the power traded to TVA for this curtailable and interruptible power. The fixed costs of investment, operation, and maintenance for these plants do not cease when TVA curtails delivery to Alcoa under the contractual arrangements.

The Commission accepted the intervenors' evidence that the return entitlements result from the investment, maintenance and operation costs necessary to make the hydroelectric generation of Nantahala and Tapoco available for TVA's demands. Ultimately, the companies' approach was found to unfairly burden the public customers by requiring them to bear costs properly assignable to Alcoa for the fixed costs necessary to generate the power traded to TVA. The Commission again described the reasons why the NFA trade-off distorted customer cost responsibility, and was therefore improper to use as a basis for computing Nantahala's demand and energy costs.

> In essence, the NFA is a trade-off of certain firm power and secondary power, available less than 50% of the time, for lesser amounts of firm and secondary power that are curtailable and interruptible but available more than 50% of the time, since any power available more than 50% of the time is usable by Alcoa in its aluminum smeltering operations. *The trade-off result is a considerable improvement in the value of Tapoco's energy useable for Alcoa's aluminum production. The trade-off has no value to the public load. Alcoa (Tapoco) should, therefore, take full cost responsibility for the demand-related costs associated with the capacity traded off.*

In conclusion, the Commission stated that the companies' proposed demand allocation technique would result in a "gross ineq-

uity" to Nantahala and the public load customers, and that demand and energy charges should properly be based upon the capabilities and needs of Nantahala and Tapoco outside of the TVA return entitlements.

Next, the Commission discussed the intervenors' proposed cost allocation methodology and concluded that in view of "the entire evidence of record with respect to the assignment of cost," this method would be employed to determine Nantahala's demand and energy related costs. The data accepted by the Commission as representing the capabilities and needs of the Nantahala-Tapoco unified system appropriate for use in the allocation of demand related costs is as follows:

A. Dependable Capacity for NP&L Projects	85.4 Mw
B. Dependable Capacity of Tapoco Projects	302.8 Mw
C. Total (A + B)	388.2 Mw
D. Less Reserve at 3%	11.3 Mw
E. Net *Firm* Capacity Available to Meet the Load (C − D)	376.9 Mw
F. Purchase Power of NP&L from TVA	50.4 Mw
G. Losses on F above (assumed 5%)	2.5 Mw
H. Total Net *Firm* Capability Available at Generation to Meet the System Requirements of NP&L and Tapoco (E + F + G)	429.8 Mw

Nantahala's peak load during the test year was 105,747 kw, which figure represents its maximum need during the year. Nantahala's demand responsibility for costing purposes was then calculated by dividing the total Nantahala-Tapoco system demand responsibility into Nantahala's maximum demand responsibility. Dividing 429,800 kw into 105,747 kw produces a Nantahala demand allocation of 24.60% of the system's demand responsibility. Using this allocation factor, the Commission assigned 24.60% of the Nantahala-Tapoco unified system demand costs to Nantahala and the balance to Tapoco (Alcoa).

While demand charge allocations must be computed based upon production capacity and capacity needs, energy charge allocations must be computed based upon the average energy available for the Nantahala-Tapoco unified system plus Nantahala's separate purchases from TVA. The data accepted by the Commission as appropriate for use in the allocation of energy related costs is as follows:

A. Average Energy Available from NP&L Projects (New Fontana Agreement Apportionment Study)	391,500 Mwh
B. Average Energy Available from Tapoco's Projects (New Fontana Agreement Apportionment Study)	1,373,600 Mwh
C. Total Average Energy Available from NP&L and Tapoco's Projects (A + B)	1,765,100 Mwh
D. NP&L Purchase of Energy from TVA	81,265 Mwh
E. Losses on D above (assumed 5%)	4,063 Mwh
F. Total Average Energy Available to Meet System Load (C + D + E)	1,850,428 Mwh

Nantahala's energy requirement during the 1975 test year was 453,548 mwh. Nantahala's energy responsibility for costing purposes was then calculated by dividing the total Nantahala-Tapoco system energy responsibility into Nantahala's energy responsibility. Dividing 1,850,428 mwh into 453,548 mwh produces a Nantahala energy responsibility of 24.51%. Using this allocation factor, the Commission assigned 24.51% of the Nantahala-Tapoco unified energy costs to Nantahala and the balance to Tapoco (Alcoa).

The methods, procedures and results of the intervenors' jurisdictional cost allocation methodology were adopted by the Commission in all material respects for determining Nantahala's retail costs of service. The practical effect of basing Nantahala's costs on actual combined system capabilities and needs was a decrease in the percentage of costs associated with the NFA and 1971 Apportionment Agreement recoverable from Nantahala's retail rate payers. The other "costs" actually incurred by the

unified system under the agreements were effectively allocated for rate making purposes to the systems' industrial customer, Alcoa, on whose behalf the Commission determined they were incurred.

To summarize, this matter was remanded for the purpose of determining whether a roll-in methodology was appropriate for Nantahala and Tapoco. Having determined that it was, and having identified those total system costs related to the supply of energy and those related to the demand for energy, the Commission was left with the task of allocating the appropriate demand and energy costs as between the North Carolina and Tennessee jurisdictional customers. The Commission then adopted the technique of cost allocation proposed by the intervenors' witness Springs, and allocated 24.60% of the combined demand costs and 24.51% of the combined energy costs to Nantahala's cost of service. These Nantahala percentages are calculated upon the relative contributions and needs of Nantahala as part of a combined system and not upon how Nantahala and Tapoco share in the N Fontana Agreement entitlements under the 1971 Apportionm Agreement. Although those contracts limit and rearrange the system's "energy" and "demand" availability, they do not allocate "cost of service" percentages between the retail consumers of the combined system's power. The roll-in and allocation of total system costs merely allowed the Commission to assign customer cost responsibility on the features of the actual system and not the system as reshaped by the New Fontana Agreement. The method does not ignore or alter the results of that agreement, it determines who is to bear the responsibility for the costs associated with the facilities and resources obligated thereunder. Having decided that Alcoa in negotiating the NFA effectuated a trade-off of dependable hydro capacity in return for improving the availability of energy for aluminum production, the Commission concluded that the aluminum production load should be assigned the responsibility for the investment costs and operation and maintenance expenses of the generating facilities for that traded capacity.

As the Commission stated in its order, one of the purposes for the roll-in method of rate making is to "cancel" or at least to "true up" the concealed benefits it found flowing to Alcoa under the power supply agreements. This is but another way of stating

that one purpose of the roll-in is to assign the appropriate cost responsibility for the respective customer demands upon the combined system's power supply resources. Obviously, use of the entitlements contained in these agreements, which do not reflect the investment costs and operation and maintenance expenses of the generating facilities upon which customer cost responsibility must be calculated, to then allocate costs would defeat the very purpose of the roll-in.

Moreover, as Nantahala itself recognizes in its brief, "the 1971 Apportionment Agreement is premised on the fact that Nantahala and Tapoco are separate entities and that the entitlements allocated to Nantahala *are deemed to arise* in exchange for Nantahala's generation just as the entitlements allocated to Tapoco *are deemed to arise* in exchange for Tapoco's generation." (Emphasis added.) The Commission, in rejecting the fiction that Nantahala and Tapoco were developed, designed and operated as separate corporate entities, also rejected the fiction that return entitlements *deemed to arise* in exchange for the value of the generation turned over to TVA can be used as accurate measures of the demand and energy related costs fairly attributable to Nantahala's provision of service to its retail rate payers.

It was the position of the intervenors' expert witness that the system-wide trade-off of costs and benefits under the NFA and 1971 Apportionment Agreement was detrimental to Nantahala's ability to provide service at just and reasonable rates to its public customers and unfairly shifted costs within the system to Nantahala which are properly attributable to Alcoa. Based upon substantial evidence of record, the Commission adopted this position and the roll-in technique proposed to measure and assign customer cost responsibility for the combined system's hydroelectric resources. The roll-in technique chosen by the Commission is fully supported by substantial evidence of record and is a determination which essentially rests within the discretion of the Commission in the exercise of its rate making function. As the United States Supreme Court has observed in reviewing a similar regulatory question, "judgment and discretion control both the separation of property and the allocation of costs when it is sought to reduce to its component parts a [utility] business which functions as an integrated whole." *Colorado Interstate Gas Co. v. FPC,* 324 U.S. at 591, 89 L.Ed. at 1217.

The companies do not argue, nor do we find, any error in judgment or abuse of discretion in the action of the Commission in the Sub 29 (Remanded) proceedings regarding the mechanics of the roll-in or the allocation formula utilized. Briefly stated, the principal arguments advanced by the companies are that the roll-in was impermissible under the doctrine of federal preemption because the two principal power supply contracts at issue are regulated by the FERC and that federal law prohibits the results obtained by the Commission under the roll-in as an undue burden on interstate commerce. We turn next to these and other remaining arguments of the companies concerning the order appealed from.

II.

A.

The New Fontana Agreement and its predecessor, the Original Fontana Agreement, effectuate power exchanges between Nantahala, Tapoco and TVA falling within the regulatory jurisdiction of the FERC under Part II of the Federal Power Act. Sections 205 and 206 of the Act, 16 U.S.C. §§ 824d and 824e, give FERC the authority to regulate wholesale rate schedules for the sale of electricity in interstate commerce. As we have seen, the OFA was never filed with FERC's predecessor, the FPC, as a tariff or rate schedule and the FPC never ruled upon the substantive terms of that agreement. The NFA was filed with the FPC "under protest" by Tapoco and Nantahala in response to the FPC's request that the companies do so. The NFA was formally designated "Tapoco Rate Schedule No. 3" and "Nantahala Rate Schedule No. 1" in 1966. No substantive review of its terms was undertaken by the FPC until Nantahala's wholesale customers raised the matter in 1978. The 1971 Apportionment Agreement, a contract affecting rates and charges under the Act, was not filed with the FPC until 1980, in conjunction with the foregoing complaint by Nantahala's customers. The contract was then designated as "Supplement 2 to Tapoco Schedule 3" and as a "Supplement to Nantahala Schedule No. 1." Again, substantive review of the operative effect of this agreement upon Nantahala's wholesale rates was not undertaken by FERC until 1980.

[7] Now, at the close of a forty year period marked by an "apparent determination never willingly to submit any of its hydro

projects to the duly enacted requirements of Federal law," 2 F.P.C. at 390, Nantahala and Alcoa argue, in effect, that FERC's exclusive jurisdiction to regulate interstate wholesale power transactions and to set wholesale rates preempts the North Carolina Utilities Commission from implementing a jurisdictional cost allocation formula which fails to utilize the proportion of NFA demand and energy entitlements allocated to Nantahala under the 1971 Apportionment Agreement in determining Nantahala's retail costs of service. Before addressing the separate and specific contentions of the companies, we will briefly review the legal and regulatory framework under which these issues arise.

1.

The doctrine of preemption is based upon the Supremacy Clause of the United States Constitution. U.S. Const., art. VI, cl. 2. When Congress legislates in an area within the federal domain, it may, if it chooses, take for itself all regulatory authority over the subject, share the task with the states, or adopt as federal policy the state scheme of regulation. *Rice v. Santa Fe Elevator Corp.*, 331 U.S. 218, 91 L.Ed. 1447 (1947). The question in each case is the intent of Congress. *Id.* As the United States Supreme Court recently observed, "[m]aintaining the proper balance between federal and state authority in the regulation of electric and other energy utilities has long been a serious challenge to both judicial and congressional wisdom. On the one hand, regulation of utilities is one of the most important of the functions traditionally associated with the police power of the States. . . . On the other hand, the production and transmission of energy is an activity particularly likely to affect more than one State, and its effect on interstate commerce is often significant enough that uncontrolled regulation by the States can patently interfere with broader national interests." (Citations omitted.) *Arkansas Elec. Coop. Corp. v. Arkansas Public Serv. Comm.*, 461 U.S. 375, 377, 76 L.Ed. 2d 1, 6 (1983). The Federal Water Power Act, now Part I of the Federal Power Act, 16 U.S.C. §§ 791a-823a, was enacted by Congress under its Commerce Clause powers in 1920. *New England Power Co. v. New Hampshire*, 455 U.S. 331, 340, 71 L.Ed. 2d 188, 196 (1982). The potential of water power as a source of electric energy led Congress to exercise its constitutional authority over navigable streams to regulate and encourage development of hydroelec-

tric power generation "to meet the needs of an expanding economy." *Id.* at 340, 71 L.Ed. 2d at 196, *quoting FPC v. Union Electric Co.*, 381 U.S. 90, 99, 14 L.Ed. 2d 239, 246 (1965).

Part II of the Federal Power Act, 16 U.S.C. §§ 824-824k, was enacted by Congress in 1935 as a "direct result" of the Supreme Court's holding in *Public Utilities Comm'n v. Attleboro Steam & Electric Co.*, 273 U.S. 83, 71 L.Ed. 54 (1927) that the states lacked power to regulate the rates governing interstate sales of electricity for resale. It delegated to the FPC, now the FERC, exclusive authority to regulate the transmission and sale at wholesale of electric energy in interstate commerce, without regard to source of production. *New England Power Co. v. New Hampshire*, 455 U.S. 331, 71 L.Ed. 2d 188. This portion of the Act was intended to "fill the gap" created by *Attleboro* with the establishment of exclusive federal jurisdiction over such sales. *Id.*

> What Congress did was to adopt the test developed in the *Attleboro* line which denied state power to regulate a sale "at wholesale to local distributing companies" and allowed state regulation of a sale at "local retail rates to ultimate consumers."
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> . . . Congress meant to draw a bright line easily ascertained, between state and federal jurisdiction making unnecessary . . . case-by-case analysis. This was done in the Power Act by making FPC jurisdiction plenary and extending it to all wholesale sales in interstate commerce except those which Congress has made explicitly subject to regulation by the States.

FPC v. Southern Cal. Edison Co., 376 U.S. 205, 214, 215-16, 11 L.Ed. 2d 638, *reh. denied*, 377 U.S. 913, 12 L.Ed. 2d 183 (1964), *quoting Illinois Natural Gas Co. v. Central Illinois Pub. Serv. Co.*, 314 U.S. 498, 504, 86 L.Ed. 371, 375 (1942).

Exclusive federal jurisdiction in setting wholesale power rates was thought necessary because concurrent, conflicting state regulation "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress." *Chicago and N.W. Transp. Co. v. Kaylo Brick & Tile Co.*, 450 U.S. 311, 317, 67 L.Ed. 2d 258, 265 (1981). A state's independent assessment of

wholesale, interstate rates "could seriously impair the Federal Commission's authority to regulate a field over which Congress has given the Federal Power Commission [FERC] paramount and exclusive authority." *Northern Gas Co. v. Kansas Comm'n*, 372 U.S. 84, 92, 9 L.Ed. 2d 601, 608 (1963).

[8] Thus, FERC is prohibited from regulating intrastate retail rates charged to ultimate consumers and the states are prohibited from regulating interstate wholesale rates charged to local distributing companies. The result is a blend of federal-state regulation, each body with exclusive authority in its respective field. *Narragansett Electric Co. v. Burke*, 119 R.I. 559, 381 A. 2d 1358 (1977), *cert. denied*, 435 U.S. 972, 56 L.Ed. 2d 63 (1978); *Public Serv. Co. of Colo. v. Public Utils. Comm'n of Colo.*, 644 P. 2d 933 (Colo. 1982).

[9] Wholesale rates charged under the Federal Power Act must be "just and reasonable." 16 U.S.C. § 824d(a). Utilities regulated by the act are required to file rate schedules with the FERC, which has authority to investigate and modify new schedules. 16 U.S.C. § 624d(b) and (d). As a result of FERC's exclusive power to establish reasonable rates for utilities subject to its jurisdiction, a utility subject to FERC jurisdiction "can claim no rate as a legal right that is other than the filed rate, whether fixed or merely accepted by the [FERC], and not even a court can authorize commerce in the commodity on other terms. [T]he right to a reasonable rate is the right to the rate which the [FERC] files or fixes. . . ." *Montana-Dakota Util. Co. v. Northwestern Pub. Serv. Co.*, 341 U.S. 246, 251, 95 L.Ed. 912, 919 (1951). Thus, the North Carolina Utilities Commission is preempted from directly or indirectly regulating the wholesale rate structure created by the New Fontana and 1971 Apportionment Agreements or inquiring into the reasonableness of those FERC-filed wholesale rate schedules when it acts in fixing Nantahala's retail rates.

Nantahala and Alcoa present a number of overlapping and somewhat confused arguments regarding their contention that the doctrine of federal preemption stands as a bar to the Commission's order. It appears, however, that in essence both Nantahala and Alcoa argue that the Commission has directly interfered with FERC's exclusive and paramount jurisdiction over the NFA and 1971 Apportionment Agreement by reviewing the reasonableness

of these contracts and has indirectly intruded upon that jurisdiction by disregarding or altering the level of costs and expenses attributed to Nantahala as if it were a stand-alone company under these contracts. We disagree.

With respect to the former argument, it is clear that the Commission's examination of the NFA and 1971 Apportionment Agreement was not undertaken in an effort to either establish wholesale rates or to modify agreements filed with and approved by the FERC. In its order reducing rates the Commission expressly rejected the remedy of reforming these agreements to award Nantahala its just level of entitlements and nothing contained in the Commission's order purports to change or modify a single word of the several contracts or agreements involved, or the actual flow of power thereunder.

The companies rely heavily upon the holdings in *Attleboro* and *Southern California Edison* to challenge the authority of the Commission to implement the roll-in methodology proposed by the intervenors. We find that reliance to be misplaced. In each of those cases the dispositive fact under the doctrine of federal preemption was the state commission's specific modification of a contract establishing a wholesale rate. In the instant case, neither the contracts themselves nor the wholesale rates fixed thereunder were changed by the Commission in its order. The roll-in was used solely to determine the unified rate base, operating costs and revenues of Nantahala and Tapoco and to allocate jurisdictional costs of service in the process of fixing Nantahala's retail rates to its North Carolina consumers. *Attleboro* and *Southern California Edison* confirm, rather than deny, the propriety of state regulation of retail electric power rates.

Nor are we persuaded by the companies' arguments that the Commission has indirectly intruded upon the federal regulatory domain by disallowing or altering the interstate wholesale costs and expenses borne by Nantahala under the NFA and the 1971 Apportionment Agreement. Rather, we find the Commission's treatment of those wholesale costs to be well within the field of exclusive state rate making authority engendered by the "bright line" between state and federal regulatory jurisdiction under the Federal Power Act.

The Utilities Commission is the administrative agency charged with the duty of regulating the intrastate retail rates of public utilities within the State of North Carolina. N.C.G.S. § 62-32. Under N.C.G.S. Chapter 62, the Commission is authorized to conduct hearings to investigate the propriety of proposed rate changes and to make such orders with regard to the proposed rate as may be just and reasonable. In fixing rates under N.C.G.S. § 62-133, the Commission must fix such rates "as shall be fair to both the public utility and to the consumer." N.C.G.S. § 62-133(a). The basic theory of utility rate making pursuant to that statute is that rates should be fixed at a level which will recover the cost of service to which the rate is applied, plus a fair return to the utility. *Utilities Comm. v. Edmisten, Atty. General*, 291 N.C. 451, 232 S.E. 2d 184 (1977). This provision of Chapter 62 lays down the procedure by which the Commission is to fix rates "which will enable the utility 'by sound management' to pay all of its costs of operation, including maintenance, depreciation and taxes, and have left a fair return upon the fair value of its properties." *Utilities Comm. v. Telephone Co.*, 285 N.C. 671, 680-81, 208 S.E. 2d 681, 687 (1974). However, the primary purpose of Chapter 62 is to assure the public of adequate service at a reasonable charge; the provisions of this Chapter designed to assure the utility of adequate revenues are in the nature of corollaries to the basic proposition that the public is entitled to adequate service at reasonable rates. In addition such "corollaries" act as safeguards against arbitrary and unconstitutional administrative action. *Id.*

N.C.G.S. § 62-133 prescribes the formula which the Commission is required to follow in fixing rates for service to be charged by any public utility in pertinent part as follows:

> (b) In fixing such rates, the Commission shall:
>
> (1) Ascertain the reasonable original cost of the public utility's *property used and useful . . . in providing the service rendered to the public within* this State. . . .
>
> * * *
>
> (3) Ascertain such public utility's reasonable operating expenses, including actual investment currently consumed through reasonable actual depreciation. (Emphasis added.)

The fair value of the property described in paragraph (b)(1) is the rate base. Additionally, paragraph (c) of this statute allows the consideration of evidence of changes in costs, revenues, or the cost of the public utility's property used and useful "in providing the service rendered to the public within this State," within a reasonable time after the test period.

[10] Clearly, the statute limits the property upon which the North Carolina consumers are required to pay a return to the property used and useful in providing *intrastate* service. When the provisions of N.C.G.S. § 62-133(b)(1), (b)(3) and (c) are read *in pari materia, see Utilities Commission v. Duke Power Co.*, 305 N.C. 1, 287 S.E. 2d 786 (1982), it is apparent that the only operating expenses which the Commission may consider in setting intrastate rates for North Carolina public utilities are those incurred in the provision of service to the utility's North Carolina consumers. *See, e.g., Utilities Comm. v. Edmisten, Attorney General*, 291 N.C. 424, 430, 230 S.E. 2d 647, 651 (1976) (system-wide cost of service study which significantly varied from results produced by a study based solely on North Carolina data would be incompetent since, "North Carolina rates may not be structured by external system usage"); *Utilities Comm. v. Telephone Co.*, 281 N.C. 318, 366, 189 S.E. 2d 705, 751 (1972) ("'North Carolina users of telephones are not to be required to furnish revenue to maintain applicant's financial condition which other states refuse to provide'"); *Utilities Commission v. State of North Carolina*, 239 N.C. 333, 345-46, 80 S.E. 2d 133, 141 (1954) ("Strictly speaking what is the fair value of applicant's investment in its intrastate business in this State and what constitutes a fair return thereon are the primary questions before the Commission for decision"). Accordingly, jurisdictional cost allocation is a necessary step in any general rate case involving a public utility or utility system whose separate companies are operated as a single enterprise serving both jurisdictional (intrastate retail) and non-jurisdictional consumers. *See also Colorado Interstate Gas Co. v. FPC*, 324 U.S. 581, 89 L.Ed. 1206.

[11] Additionally, in construing the provisions of N.C.G.S. § 62-133, the Commission must also consider section (d) of that statute, which provides that the "Commission shall consider all other material facts of record that will enable it to determine what are reasonable and just rates." N.C.G.S. § 62-133(d) has been construed as a device permitting the Commission to take action consistent with the overall command of the general rate statutes, but not specifically mentioned in those portions of the statute under consideration in a given case. *See, e.g., Utilities Commission v. Duke Power Co.*, 305 N.C. 1, 287 S.E. 2d 786 (Commission correctly considered non-statutory material factor concerning depreciation expenses in determining what are reasonable and just rates pursuant to N.C.G.S. § 62-133(d)). *See also Utilities Commission v. Public Staff*, 58 N.C. App. 453, 293 S.E. 2d 888 (1982), *modified and affirmed*, 309 N.C. 195, 306 S.E. 2d 435 (1983) (Commission must take other factors such as the efficiency of the company's operations into account in fixing its rates in a general rate case). In sum, the fixing of "reasonable and just" rates involves a balancing of shareholder and consumer interests. The Commission must therefore set rates which will protect both the right of the public utility to earn a fair rate of return for its shareholders and ensure its financial integrity, while also protecting the right of the utility's intrastate customers to pay a retail rate which reasonably and fairly reflects the cost of service rendered on their behalf.

[12, 13] The fundamental question as to whether certain expenditures are to be included in the operating expenses a utility is entitled to collect from its customers is one of fact to be ascertained by the regulating authority. *See generally*, 1 Priest, *Principles of Public Utility Regulation* 45 (1969). "If properly incurred, they must be allowed as part of the composition of the rates. Otherwise, the so-called allowance of a return upon the investment, being an amount over and above expenses, would be a farce." *Mississippi River Fuel Corp. v. FPC*, 163 F. 2d 433, 437 (1947). *Accord Narragansett Electric Co. v. Burke*, 119 R.I. 559, 381 A. 2d 1358. As a corollary to the foregoing proposition, it is also true that ordinarily, the Commission may, in a proper case, refuse to allow the utility to include in its reasonable operating expenses, the full price it actually paid for power as a result of its contractual power supply arrangements. *Utilities Comm. v. Intervenor Residents*, 305 N.C. 62, 286 S.E. 2d 770 (1982). This is especially so where the operating expense being investigated by the Commission is one incurred through a contract between or including the utility company and its affiliated companies, including parent corporations and subsidiaries of parent corporations. *Id.* In such

cases the burden of persuasion on the issue of reasonableness always rests with the utility; charges arising out of intercompany relationships between affiliated companies should be scrutinized with care and may be properly refused or disallowed in the absence of a showing of their reasonableness. *Id.*; *Utilities Comm. v. Telephone Co.*, 281 N.C. 318, 189 S.E. 2d 705.

[14] A major operating expense which the Commission must necessarily consider in arriving at reasonable and just rates for Nantahala is the "cost" of power Nantahala incurs under the power supply agreements with its affiliates and TVA. However, the Commission's otherwise plenary authority to investigate transactions between a public utility and its affiliated companies, and to disallow operating expenses found to be imprudently incurred or allocated under such agreements, is limited by prior federal approval of the rate or price in question under the "filed rate" doctrine of *Montana-Dakota Util. Co. v. Northwestern Pub. Serv. Co.*, 341 U.S. 246, 95 L.Ed. 912. There, the United States Supreme Court stated:

> We hold that the right to a reasonable rate is the right to the rate which the Commission files or fixes, and that, except for review of the Commission's orders, the courts can assume no right to a different one on the ground that, in its opinion, it is the only or the more reasonable.

Id. at 251-52, 95 L.Ed. at 919. Thus, neither the state public service commission nor the courts can unilaterally establish a different rate for wholesale electric power sold in interstate commerce because they are of the opinion that the FERC-filed or approved rate is unfair or unreasonable. *See Public Serv. Co. of Colo. v. Public Utils. Comm'n of Colo.*, 644 P. 2d 933.

Those state courts which have considered the question have uniformly agreed that a utility's costs based upon a FERC-filed rate must be treated as a reasonably incurred operating expense for the purposes of setting an appropriate retail rate. *Narragansett Electric Co. v. Burke*, 119 R.I. 559, 381 A. 2d 1358; *Public Serv. Co. of Colo. v. Public Utils. Comm'n of Colo.*, 644 P. 2d 933; *United Gas Corp. v. Mississippi Pub. Serv. Comm'n*, 240 Miss. 405, 127 So. 2d 404 (1961); *City of Chicago v. Illinois Commerce Comm'n*, 13 Ill. 2d 607, 150 N.E. 2d 776 (1958); *Citizen Gas Users Ass'n v. Public Util. Comm'n*, 165 Ohio St. 536, 138 N.E. 2d

383 (1956); *Eastern Edison Co. v. Dept. of Public Util.*, 388 Mass. 292, 446 N.E. 2d 684 (1983); *Pike Cty. Light & Power v. Pennsylvania*, 465 A. 2d 735 (Pa. Cmwlth. 1983); *Washington Gas Light Co. v. Public Serv. Comm'n*, 452 A. 2d 375 (D.C. App. 1982), *cert. denied*, 462 U.S. 1107, 77 L.Ed. 2d 1334 (1983). "Otherwise, a State utilities commission could review the reasonableness of the FERC-filed wholesale rate in a proceeding establishing retail rates, in violation of the Federal Power Act." *Eastern Edison Co. v. Dept. of Public Util.*, 388 Mass. at 300, 446 N.E. 2d at 689; *Northern States Power Co. v. Minnesota P.U.C.*, 344 N.W. 2d 374 (Minn.), *cert. denied, Humphrey v. North States Power Co.*, --- U.S. ---, 82 L.Ed. 2d 850 (1984); *Northern States Power Co. v. Hagen*, 314 N.W. 2d 32 (N.D. 1981); *Office of Public Counsellor v. Indiana & Michigan Electric Co.*, 416 N.E. 2d 161 (Ind. App. 1961). *See also Northern Gas Co. v. Kansas Comm'n*, 372 U.S. 84, 9 L.Ed. 2d 601. *See generally*, 16 A.L.R. 4th 454, § 3(b).

Nantahala and Alcoa rely heavily upon the foregoing line of cases in support of their arguments that the utilization of the roll-in in the instant case violates the Supremacy Clause of the United States Constitution because it is inconsistent with federal jurisdiction over the NFA and the 1971 Apportionment Agreement. The companies contend, in effect, that the Commission's failure to base Nantahala's demand and energy related costs on the quantity and design of entitlements assigned to Nantahala on a stand-alone basis under these agreements is tantamount to a disallowance of costs actually borne by Nantahala and as such constitutes an impermissible, indirect intrusion into the federal regulatory domain. We reject the companies' various federal preemption arguments for two reasons: (1) their reliance upon the *"Narragansett-Northern States"* line of authority to establish a Supremacy Clause violation is misplaced and (2) their arguments rest upon the faulty premise that FERC deemed both the NFA and the 1971 Apportionment Agreement to be fair and reasonable to Nantahala, when in fact it expressly ruled that the latter agreement was "unfair" and refused to permit Nantahala to base its requested wholesale rate increase upon the costs incurred thereunder.

The rule requiring state commissions to "treat" costs based upon FERC-filed rates as reasonably incurred operating expenses, thus preventing the automatic disallowance of these costs, has not

been held to preclude state authority to determine whether these costs should be automatically passed through to retail consumers in the form of higher rates. For example, in the *Narragansett* case itself, the Rhode Island Supreme Court concluded that although the state utilities commission had to consider the cost of electricity to the local distributing company based upon its supplier's federally filed wholesale rate as an actual operating expense, it was not required to adjust Narragansett's retail rates to reflect the increased wholesale costs under its PPCA (Purchased Power Cost Adjustment) provisions. The court reasoned that in view of the state utilities commission's broad discretion over the operation of the PPCA under the applicable state statutes and the PPCA provisions, the commission was free to "treat the proposed rate increase as it treats other filings for charged rates under [state statute] and investigate the overall financial structure of Narragansett to determine whether the company has experienced savings in other areas which might offset the increased price for power." 119 R.I. at 568, 381 A. 2d at 1363.

The Colorado Public Utilities Commission and the Colorado Supreme Court have stated even more explicitly that state commissions have the authority to determine that certain FERC-regulated wholesale costs are not incurred for the benefit of retail customers and therefore need not be passed on to retail customers in their rate schedules. *In Re Western Slope Gas Co.*, 31 P.U.R. 4th 93 (Colo. PUC 1979), *aff'd, Public Serv. Co. of Colo. v. Public Utils. Comm'n of Colo.*, 644 P. 2d 933, a natural gas utility sought to pass through the costs of its wholesale gas purchases in retail rates by means of purchased gas adjustment clauses. These costs, including surcharges to cover expenses of the Gas Research Institute ("GRI"), a research and development firm supported by the natural gas industry, were regulated by FERC. The Colorado Commission conceded that it was obligated to treat these costs as reasonably incurred operating expenses. However, the commission refused to allow the costs to be flowed through automatically to retail customers, stating that under *Narragansett*, it was free to determine whether those costs should be reflected in retail rates. 31 P.U.R. 4th at 107. The Colorado commission questioned the propriety of forcing retail customers to bear the expense due to their inability to exercise control over the expenditure of GRI

funds and because most of the benefits would flow to the gas utilities themselves and to other related private interests.

The Colorado Supreme Court upheld the commission's decision that these GRI expenses need not be passed through automatically to consumers. The court concluded that although FERC-regulated GRI expenses must be treated as reasonable and prudent operating expenses, the state commission had the authority to scrutinize such costs in a general rate case "to balance the interests of the utility investors and the ultimate consumers in arriving at a just and reasonable rate. . . ." 644 P. 2d at 941. The Colorado Supreme Court specifically recognized the Colorado commission's concern that GRI costs benefit a utility and its shareholders far more than the utility's customers. *Id.* at 941, n. 10. The court concluded its opinion by stating, "[s]o long as the PUC considers the GRI adjustment charge as a reasonably incurred operating expense of a local distribution company, as it is legally required to do, its decision to refrain from automatically passing such charges on to the ultimate consumers falls within its administrative discretion." *Id.* at 942.

In *Washington Gas Light Co. v. Public Serv. Comm'n*, 452 A. 2d 375, the District of Columbia Court of Appeals faced the same question considered in *Public Serv. Co. of Colorado*. That is, whether increases including GRI expenses reflected in a utility's FERC-regulated wholesale gas costs should be passed through to retail customers in the form of a rate increase. The local commission had disallowed the increased GRI charges as reasonable operating expenses on the grounds that FERC's authority to approve these charges was the subject of an appeal pending at the time of the commission's decision and so the costs attributed thereto were not a "measurable and certain expense." 452 A. 2d at 385. The court reversed the commission's refusal to allow the increased GRI charges to be reflected in retail rates based upon its own independent inquiry into the reasonableness of the GRI charges on the grounds that the commission was without authority to disregard a FERC order which had not been stayed during proceedings for review and was therefore in full force and effect. *Id.* at 386.

However, in the course of its discussion, the court made it quite clear that it remained within the local commission's authori-

ty to determine that the expenses should not automatically be passed through to retail customers.

> FERC's jurisdiction [does not extend] to the issue of whether increased wholesale costs shall be passed through to retail customers by the local utility. The determination of the extent to which wholesale costs should be reflected in local utility rates lies exclusively with local utility commissions. *See* [*Narragansett*].

Id. at 385, n. 15. *Accord Pike Cty. Light & Power v. Pennsylvania*, 465 A. 2d 735, 738 (FERC's jurisdiction extends to the setting of rates for out-of-state parent utility to charge local electric utility at wholesale; however, state utility commission has exclusive jurisdiction, as a matter of retail rate making, to determine whether it was just and reasonable for local utility to incur the parent's rates and charges as an expense of operation in light of available alternatives); *Kansas-Nebraska Natural Gas Co., Inc. v. State Corporation Commission*, 4 Kan. App. 2d 674, 610 P. 2d 121 (1980) (FERC's regulation of an advance payment contract with an affiliate does not preclude state public service commission's scrutiny of the agreement to determine, not whether the agreement was reasonable, but whether it was *required* for service to the local rate payers). *See also Eastern Edison Co. v. Dept. of Public Util.*, 388 Mass. 292, 446 N.E. 2d 684 (*Narragansett* and *Public Service Co. of Colorado* discussed with approval although holdings distinguished on the grounds that the Massachusetts statutes require automatic flow-through of all reasonably incurred fuel and purchased power expenses; Massachusetts commission had no authority to consider factors other than the companies' fuel costs).

Thus, several cases in the *Narragansett* line expressly recognize that a state commission retains the discretion to do exactly what the Commission has done in the instant case: determine that certain of a utility's costs were effectively incurred for the benefit of its shareholder, not its retail consumers, and therefore should be borne by the shareholder, and not by the utility's retail rate payers. The cases upon which Nantahala and Alcoa place principal reliance, *Northern States Power Co. v. Hagen*, 314 N.W. 2d 32, the related case of *Northern States Power Co. v. Minnesota P.U.C.*, 344 N.W. 2d 374, and *Office of*

Public Counsellor v. Indiana and Michigan Electric Co., 416 N.E. 2d 161, do not lead to a different conclusion.

Both *Northern States* cases involved an agreement which allocated losses incurred by an interstate utility enterprise operating in Minnesota and Wisconsin, when the Tyrone Nuclear Power Project (to be located in Wisconsin) was abandoned. The parties to the agreement, Northern States Power (NSP), a Minnesota corporation, and its wholly-owned subsidiary, Northern States Power-Wisconsin (NSP-W), a Wisconsin corporation, served, respectively, electric customers in four states, with NSP serving Minnesota, North Dakota and South Dakota and NSP-W serving only Wisconsin. Although NSP and NSP-W both originally owned an interest in Tyrone, NSP transferred its share in the project to NSP-W to comply with Wisconsin law. The transfer did not effect any change in the planned use of the project to serve the single system's various customers. NSP and NSP-W operated under the aforementioned Coordinating Agreement (CA), filed with FERC, by which they shared the total system cost of power generation in a ratio roughly proportionate to the ultimate use by the customers of each. The companies filed an amendment to the CA which was designed to allocate Tyrone abandonment costs under the same allocation formula by which the companies' wholesale rates are computed. FERC ultimately approved the amendment to the CA. Thereafter, NSP sought to "pass through" the Tyrone losses to its retail rate payers in its respective service areas, claiming that FERC's approval of the amended CA resulted in the establishment of an interstate wholesale rate which state commissions were preempted from reviewing for the purpose of retail rate making. However, both the North Dakota Public Service Commission and the Minnesota Public Utilities Commission rejected NSP's arguments that FERC approval of the amended CA automatically required the state commissions to allow NSP to treat its share of the Tyrone losses as a reasonable operating expense to be borne by NSP's North Dakota and Minnesota retail rate payers. The supreme courts of both states reversed the orders of their respective state commissions disallowing the Tyrone-related costs on the ground that the reasonableness of a formula wholesale rate filed and approved by FERC cannot be relitigated in a retail rate proceeding before a state utilities commission.

In *Northern States Power Co. v. Hagen*, the North Dakota court noted that NSP is required by the FERC order to pay a fixed wholesale rate for electricity to NSP-W which includes the amortization of the Tyrone losses. 314 N.W. 2d at 37. The court reasoned that since the North Dakota Public Service Commission had no direct jurisdiction over the interstate wholesale rates, "it would undermine the supremacy clause and the preemption doctrine for the PSC to indirectly assert jurisdiction over the wholesale rates by investigating the reasonableness of underlying [wholesale] costs in a proceeding involving retail rates." *Id.* at 38. The court concluded by stating that for purposes of fixing intrastate rates, the PSC must treat costs incurred under NSP's filed interstate wholesale rates as reasonable operating expenses. The Supreme Court of Minnesota, when faced with the identical question in *Northern States Power Co. v. Minnesota P.U.C.*, came to the identical conclusion and held that the Minnesota Public Utilities Commission was required to treat the Tyrone-related costs incurred under the FERC-approved wholesale rate formula as expenses for power purchased in determining retail rates. 344 N.W. 2d at 382.

It is thus evident that the *Northern States* cases are clearly distinguishable from the instant case in that they both involved the direct disallowance by the respective state commissions of wholesale costs approved by FERC in the exercise of its exclusive rate making authority. As we have previously stated, the Commission did not disallow any of the system costs incurred by both Nantahala and Tapoco under the NFA and 1971 Apportionment Agreement in determining the aggregate rate base and operating expenses of the rolled-in system. Rather, *all costs* attributed to Nantahala and Tapoco were *recognized and allowed* by the roll-in; the difference between "book" costs and "reasonable" costs resulting from the Commission's discretionary determination that only a certain percentage of Nantahala's book costs were incurred in serving the combined system's intrastate retail customers.

For similar reasons, we find the companies' reliance upon *Office of Public Counsellor v. Indiana & Michigan Electric Co.* to be misplaced. Again, the challenged action by the state public service commission in that case was the disallowance of a particular purchased power expense incurred by the local Indiana utility, Indiana & Michigan Electric Co. (I&M), under an interstate, wholesale power agreement with its wholly-owned subsidiary, Indiana & Michigan Power Co. (IMP). IMP's principal assets are two nuclear power production units located in Michigan. IMP's total output of electric power is sold to I&M pursuant to a FERC-regulated power agreement which provides that I&M is entitled to all of the energy generated by IMP units, and in return, I&M is obligated to compensate IMP for all costs of production and purchase power, including a return on equity. The Public Service Commission of Indiana determined that the property of the Michigan subsidiary was "used and useful" in serving the customers of the parent local utility and should therefore be included in its rate base.

In reversing that decision, the Indiana court placed great emphasis on the fact that the contract by which the parent purchased the electricity from the subsidiary, which was subject to the exclusive jurisdiction of the FERC, included a provision specifically allowing the subsidiary a return on its equity so that a "fair rate of return under the contract is computed by the FERC." *Office of Public Counsellor*, 416 N.E. 2d at 164. Thus, the court concluded that for the state commission to include the subsidiary's assets in the parent's rate base would permit the state commission to determine a cost of service and rate of return for the subsidiary *other than* the FERC established rate and would constitute an impermissible collateral attack on the authority of the FERC.

> The FERC and the Commission do not share concurrent jurisdiction with regard to the proper rate of return on IMP assets. Rather, the FERC has exclusive jurisdiction over the regulation of wholesale interstate power sales. Any attempt by the Commission to assign a rate of return attributable to IMP's cost of power clearly encroaches upon the FERC's duties and powers.

Id. at 165.

Nantahala relies on the Indiana decision in support of its argument that the Commission's "attempt to roll-together Nantahala and Tapoco and allocate a lower level of costs and expenses to Nantahala than Nantahala actually incurs under the NFA and 1971 Apportionment Agreement constitutes an intrusion upon FERC jurisdiction over those agreements, similar in

nature to the discredited 'roll-in' of I&M and IMP by the Indiana Commission." We do not agree. Again, the roll-in of Nantahala and Tapoco resulted in no disallowance or alteration of FERC-approved costs, expenses or rates of return. Nantahala's retail rates could be lowered because a lesser quantum of higher cost Nantahala energy has been averaged with a higher quantum of lower cost Tapoco energy. As a result, the average cost of roll-in energy is lower than the cost of Nantahala-only energy. Moreover, it is obvious that the "roll-in" attempted by the Indiana commission entailed a far more direct intrusion into FERC's regulatory domain in the form of a redetermination of the FERC-established rate of return for IMP's property, which fell exclusively under FERC's jurisdiction by the very terms of the interstate power agreement. Here, FERC has no authority, either exclusive or concurrent, to determine Nantahala's rate of return on its assets or the costs of service associated with providing Nantahala's intrastate retail customers with electricity. Rather, these determinations fall within the exclusive rate making jurisdiction of the North Carolina Utilities Commission.

Indeed, state commissions have been held to expressly retain, under the "filed rate" doctrine, the authority to decline to automatically reflect operating expenses incurred under FERC-regulated rate schedules or contracts in the structure of intrastate retail rates where, for example, the state commission determines (1) that increases in FERC-approved charges in one area of the utility's operations were not offset by economies in other areas (*Narragansett*); (2) that certain FERC-regulated costs were not, either in whole or in part, primarily incurred for the benefit of retail rate payers, but rather for the benefit of the utility's investors (*Public Serv. Co. of Colo.; Washington Gas Light Co.*); (3) that in light of available alternatives, certain FERC-approved expenses charged by a parent to the local utility were not reasonably attributable to the costs of serving local rate payers (*Pike Cty. Light & Power*); and (4) that certain FERC-regulated payments between parent and subsidiary were not required for service to the local rate payers (*Kansas-Nebraska Natural Gas Co.*).

In this case, the Commission, in carrying out its duty to determine what are reasonable and just rates for Nantahala's intrastate retail customers to pay for electric service, made a

searching examination of "all material facts of record," as it is required to do by N.C.G.S. § 62-133(d), including but not limited to, the effect of the FERC-filed power supply contracts on Nantahala's costs of service. It also considered the entire historical development of the Nantahala-Tapoco electric system and the intercorporate allocation of the costs and benefits associated therewith.

The Commission's extensive and detailed findings of fact taken as a whole effectively demonstrate that certain portions of the operating expenses Nantahala incurs under the NFA and 1971 Apportionment Agreement were not incurred for the benefit of Nantahala's retail rate payers, were not required for their service and were not offset by compensating economies or benefits in other areas of the utility's operations. In addition, the Commission determined that Nantahala's parent Alcoa, which is also the single largest customer of the combined system, had so dominated Nantahala that the utility was unable to act either in its own self-interest or in the interests of its public customers and that through its domination, Alcoa had received substantial concealed benefits, by means of the contractual and intercorporate structure of the "Alcoa power system," to the corresponding detriment of Nantahala's ability to render service at reasonable and just rates to its public customers. In this regard, the Commission determined that one of the most fundamental of the concealed benefits flowing to Alcoa under the NFA was the trading away of hydroelectric capacity suitable for serving a public load, at a time of sustained growth in that load, in return for entitlements structured to be of far more value for aluminum smelting than for public service.

Accordingly, the Commission determined that to the extent that Alcoa had caused Nantahala to trade capacity and energy suitable and usable for serving its public load, the costs associated with that trade-off would be borne by Alcoa and not by the retail rate payers who lost the benefit of these resources and facilities of Nantahala through intercorporate transactions over which they had no control. This determination lies well within the sphere of state regulatory authority delineated in the *Narragansett-Northern States* line of cases relied upon by the companies in support of their preemption arguments.

[15] Moreover, none of the cases relied upon by the companies dealt with the particular situation presented by the facts in this case. In effect, the Commission has recognized that two affiliated North Carolina public utilities, Nantahala and Tapoco, both of whom are controlled by their parent-customer Alcoa, itself a North Carolina statutory public utility, were in substance providing a joint service to retail customers in North Carolina, as well as to Alcoa, although the public service in North Carolina was labeled as service from Nantahala alone. By means of the roll-in, the Commission set the "Nantahala" retail rates by combining the financial data of the two affiliates into a unified rate base, and determined on a conventional load responsibility basis what portion of the rolled-in system's costs should be borne by the non-Alcoa customers, to produce the same billing rates as would result from an explicitly joint service at lawful, nondiscriminatory rates. Thus, it disregarded only the fiction of Tapoco as a separate utility system serving only Alcoa, in order to ensure that the joint Nantahala-Tapoco service to North Carolina retail customers was provided at just and reasonable rates. Insofar as the Commission determined that Alcoa as corporate parent and private industrial customer had benefited at the expense of the public load from the corporate and power supply arrangements it imposed upon its subsidiaries, it was well within its regulatory authority to decide that the costs associated with those benefits would not be borne by the public consumers in the form of higher retail rates, but would be borne by the company's customer and sole shareholder, Alcoa.

In practice, the Commission's roll-in methodology accepted Nantahala's and Tapoco's entitlements under the NFA and 1971 Apportionment Agreement, and Nantahala's supplementary purchases from TVA, as elements of the combined Nantahala-Tapoco cost of service. The Commission then determined that it was inappropriate to allow Nantahala to collect all of its revenue requirements from its public customers on the theory that it was a stand-alone company, because Nantahala's "stand-alone" costs under the corporate and contractual arrangements were not incurred for their benefit, but as a result of Alcoa's corporate dominance for Alcoa's benefit. The Commission's finding of Alcoa domination, to the extent it is based on findings of concealed benefits to Alcoa from the NFA and 1971 Apportionment Agree-

ment, is not the same as a finding that those agreements were unjust and unreasonable as wholesale rate schedules or contracts affecting wholesale rates. Rather, it is a finding that to the extent that Alcoa, rather than Nantahala and its customers benefited from those agreements, Alcoa should bear the corresponding costs (the difference between Nantahala's actual retail collections and the costs that reasonably should be borne by its retail customers).

[16] In short, contrary to the companies' assertions, the "filed rate" doctrine does not require that the Commission, in determining the proper costs to Nantahala's retail customers for the service provided to them, use demand and energy factors based upon the proportion of entitlements allocated to Nantahala alone under the NFA and 1971 Apportionment Agreement. Thus, we are unpersuaded by the arguments of Nantahala and Alcoa that this action on the part of the Commission directly or indirectly interferes with FERC's exclusive regulatory authority under the Federal Power Act.

2.

We are equally unpersuaded that the order conflicts with specific FERC actions taken with respect to the NFA and 1971 Apportionment Agreement. In fact, we find the Commission's rate making methodology to be consistent with FERC's own actions in the parallel wholesale rate case, *Nantahala Power and Light Co.*, Opin. No. 139, 19 F.E.R.C. ¶ 61,152 (1982) and Opin. No. 139-A, 20 F.E.R.C. ¶ 61,430, *affirmed on appeal, Nantahala Power and Light Co. v. FERC*, 727 F. 2d 1342.

The consolidated proceeding before the FERC involved a 1976 rate increase request filed by Nantahala and a 1978 complaint filed pursuant to Section 306 of the Federal Power Act by three of Nantahala's wholesale customers. Nantahala sought an annual rate increase based upon the test period ending 31 December 1975, effective for the period of 1 October 1976 to 1 March 1981. The customers alleged that the three companies, Alcoa, Nantahala and Tapoco, were in violation of the Federal Power Act by diverting, for the benefit and private use of Alcoa, hydroelectric power and facilities dedicated to public service. The customers argued that Alcoa had used the separate corporate identities of Nantahala and Tapoco to frustrate the purposes of the Federal Power Act, that the corporate structure and

resulting power supply agreements were unfair to Nantahala, and that the situation could be remedied by either a roll-in of Nantahala and Tapoco or by reformation of the power supply agreements to reflect a more fair and reasonable allocation of power and energy to Nantahala. Although the Administrative Law Judge rejected the single entity theory of the customers, and therefore their proposed roll-in remedy, he expressly found that the allocation of entitlements to Nantahala under the 1971 Apportionment Agreement was unfair. *See* 15 F.E.R.C. ¶ 63,014.

The ALJ concluded that it would be unjust to require Nantahala's wholesale customers to bear their proportionate share of the purchased power costs associated with the 1971 Apportionment Agreement and the Nantahala-TVA supplemental purchase contract. Instead, he determined that the rates should be set *as if* the 1971 Agreement allocated the NFA entitlements in a manner proposed by the FERC staff. Inasmuch as the rates computed on this basis were lower than the rates charged on the basis of Nantahala's book costs under those agreements, Nantahala was ordered to refund its customers the extra revenue it had collected to pay for the unnecessary TVA purchases. The ALJ also determined that Nantahala's PPAC was unlawful and that the 1971 Apportionment Agreement was a contract affecting rates and charges under Section 205(c) of the Federal Power Act, which should have been filed when made. However, the ALJ declined to impose sanctions for Nantahala's failure to timely file the agreement.

In Opinion No. 139, the FERC affirmed the ALJ's order in all material respects. *Nantahala Power and Light Company*, 19 F.E.R.C. ¶ 61,152. Once again, examination of the relevant power transactions and power supply agreements was undertaken primarily to resolve the "central question [of] whether a preponderance of the evidence supports a finding that Alcoa has used the separate corporate identities of Nantahala and Tapoco to frustrate the purposes of the Federal Power Act." *Id.* at p. 61,276. Although the FERC answered the question thus posed in the negative, and therefore rejected the customers' related contention that the two companies operate as an integrated system whose rates should be determined on a rolled-in basis, it expressly recognized that the North Carolina Utilities Commission has and may reach a different conclusion under state law on both the

status of Tapoco as a North Carolina public utility, *id.* at p. 61,277, n. 21, and on the question of rolled-in costing, *see* 20 F.E.R.C. ¶ 61.430.[21]

The FERC briefly examined the circumstances surrounding the OFA and the NFA and concluded that the two agreements were the result of "arms length bargaining" and that "[t]he above history of the OFA and NFA indicates no intent on the part of any of the parties to ignore the needs of Nantahala's public service customers or deprive them of energy at just and reasonable rates." 19 F.E.R.C. ¶ 61,152 at p. 61,278. Continuing, the FERC stated: "The apportionment agreements are another matter. . . . *The alleged fairness of the 1971 Agreement is not supported by the record.* The 1963 Agreement gave Nantahala considerably greater benefits than does the 1971 Agreement, and there is no indication in the record as to why Nantahala, without consideration, gave up those benefits." *Id.* at pp. 61,278-79. (Emphasis added.)

In affirming the decision of the ALJ, the FERC determined that Nantahala should have received a greater share of the NFA entitlements and that a disproportionate share had been assigned to Tapoco. To remedy this inequity for rate making purposes, FERC adopted the staff's calculation of a fair share of entitlements for Nantahala based upon its actual relative contribution to the total net combined generation of the two companies' plants which is turned over to TVA under the NFA (22.50%) and then determined that Nantahala should have received 22.50% (or 404 million) of the 1,800 million kwh under the 1971 Apportionment Agreement. Since Nantahala had received only 360 million kwh under the 1971 Agreement, FERC reasoned that Nantahala had purchased from TVA 44 million kwh of energy more than it should have, and that these excessive purchases should not have been reflected in Nantahala's wholesale rates. Therefore, the FERC ordered that "Nantahala shall be required to refund, with interest, any amounts collected in excess of those which would

21. In its order denying rehearing (Opinion No. 139-A), FERC stated: "We recognize that the North Carolina Utilities Commission (NCUC), based on a similar record, reached a different conclusion concerning rolled-in costing. However, the question of whether to treat various entities as an integrated system for rate making purposes is not a purely factual question, but also rests on criteria which each rate making authority may deem relevant." *Id.* at p. 61,869.

have been payable by customers had Nantahala received entitlements as described in the preceding paragraphs." *Id.* at p. 61,280.

In its order denying the rehearing requested by all parties, 20 F.E.R.C. ¶ 61,430, FERC rejected the claims of Alcoa and Nantahala that Opinion No. 139 actually reallocated the NFA entitlements and that it would result in the confiscation of Nantahala's property by setting rates below Nantahala's actual costs. FERC explained that its order merely set rates *as though* a portion of the interruptible entitlements were allocated to Nantahala:

> *In determining just and reasonable rates in Opinion No. 139, the Commission did not choose to reform the 1971 Apportionment Agreement and was not concerned with the mechanics of how entitlements of energy from TVA are allocated to each party, as long as each party receives its fair share of energy based on that party's contribution of actual energy turned over to TVA.* The mechanics of the proportions of both primary and secondary energy available from TVA rests with the parties. Our concern is that each party receive its proper entitlement. *Nantahala entered into a 1971 contract which we find unfair. As a result, the company had to make purchases from TVA which otherwise would not have had to be made. Nantahala must bear the consequences of its acts and refund rates collected to recover the costs of the excess purchases.*

20 F.E.R.C. ¶ 61,430 at p. 61,871. The practical effect of FERC's rate making methodology was the allocation to Alcoa of the "excess" costs Nantahala was forced to incur under the 1971 Agreement.

On appeal taken from the FERC's orders, the Fourth Circuit Court of Appeals held that: (1) FERC's finding that the 1971 Apportionment Agreement was unfair to Nantahala was supported by substantial evidence, and (2) the decision of FERC that a "roll-in" or consolidation of Nantahala and Tapoco for rate making purposes was *not necessary* in this instance was also supported by substantial evidence. *Nantahala Power and Light Co. v. FERC*, 727 F. 2d 1342. With respect to the latter point, the court recognized that although the evidence *did suggest* the propriety of a roll-in, the decision to order a roll-in rests within the discre-

tion of the agency charged with rate making responsibility. *Id.* at 1348. As to FERC's determination that the NFA was not unfair to Nantahala, the court adverted to the fact that "substantial weight in the NFA went to Alcoa's needs," but reasoned that that fact alone "is not conclusive proof that Alcoa sacrificed the Customers' interests to that of the Alcoa aluminum operations. It should be expected that more emphasis would be given to Alcoa's requirements than Nantahala's given the fact that Tapoco is much bigger than Nantahala, and in the early years of the NFA, even some of Nantahala's power and energy was sold to Alcoa." *Id.* at 1349.

We find a number of points particularly noteworthy with regard to the federal regulatory actions discussed above. First, FERC's entire examination of the factual issues common to both the wholesale and retail rate cases was undertaken in an effort to resolve legal issues not before the Commission and vice-versa. FERC's examination of the corporate structure of the Alcoa power system and the various intercorporate power transactions and agreements at issue was undertaken primarily in an effort to determine whether Alcoa had used the separate corporate identities of Nantahala and Tapoco to frustrate the purposes of the Federal Power Act, and having answered that question in the negative, FERC then declined to order the remedy of a roll-in.

[17] Contrary to the arguments of Nantahala and Alcoa, we conclude that FERC's analysis of the corporate structure and the various intercorporate power transactions and agreements at issue, and its finding that the evidence before it did not support the conclusion that Alcoa had used the separate corporate identities of Nantahala and Tapoco to frustrate the purposes of the Federal Power Act, does not preempt the Commission from determining that the evidence before it supports the conclusion that Alcoa had dominated Nantahala in such a manner as to require relief for Nantahala's retail customers under North Carolina law. Nor does FERC's having declined to order a roll-in of Nantahala and Tapoco for rate making purposes preempt the Commission from implementing such a rate making methodology under *its discretionary authority* in setting intrastate retail rates. Both the FERC and the Fourth Circuit Court of Appeals recognized that the decision to implement a "roll-in" (1) is based upon factors each regulatory body deems appropriate to the case before it; (2) rests within the discretion of the agency charged with such rate mak-

ing authority; and (3) is a matter upon which state and federal regulatory agencies may differ without the determination of the one necessarily binding the actions of the other.

We first observe that a fundamental factor in the differing treatment given by the federal and state regulatory bodies with respect to the NFA and the 1971 Apportionment Agreement arises out of their differing conclusions as to whether Nantahala is to be treated as a stand-alone company or as an integral unit in a single integrated and coordinated power system. The Commission's rejection of the companies' proposal to base Nantahala's energy and demand related costs on the entitlements it received under the contracts was based, in large part, on its findings that these entitlements were apportioned to Nantahala on the hypothetical and false assumption that Nantahala was developed and operated as a stand-alone utility company. No action taken by FERC may be said to preempt the Commission from rejecting a cost allocation formula based upon a factual premise that it has in turn properly rejected in the exercise of its rate making authority.

Moreover, with respect to FERC's treatment of the contracts themselves, it cannot be said that the findings of the Commission undermine an unequivocal FERC endorsement of the NFA and the 1971 Apportionment Agreement. FERC Opinion Nos. 139 and 139-A are far less inclusive in scope and approving in nature than the companies imply.

FERC did not, as both Alcoa and Nantahala repeatedly assert, find the NFA to be "just and reasonable," it merely determined that the contract was negotiated at "arms-length" and without the "intent" to "ignore" the needs of Nantahala's public customers. These findings are not tantamount to a determination that the contract equally benefits Nantahala's rate payers and Alcoa, or that its terms were required for or structured to be of benefit in service to those rate payers, which are matters the Commission was properly concerned with. More pointedly, and contrary to the assertions of Nantahala that FERC fully and unconditionally "deemed fair" the provisions of the 1971 Apportionment Agreement, FERC expressly found that agreement to be unfair to Nantahala and expressly refused to base Nantahala's rates to its wholesale customers upon the entitlements assigned to Nantahala under that agreement.

In fact, in setting those rates, FERC utilized a rate making methodology similar in principle to that implemented by the Commission—that is, FERC set Nantahala's wholesale rates on the lower level of energy related costs FERC determined Nantahala *should have* incurred given the relative contribution of its plants to the net generation Nantahala and Tapoco jointly turn over to TVA under the NFA. These determinations and the remedial rate making methodology employed by FERC were, in turn, fully affirmed by the Fourth Circuit Court of Appeals. It is therefore clear that the Commission's findings with respect to detriments Nantahala suffered by the terms of the 1971 Apportionment Agreement harmonize rather than conflict with findings by the FERC that the agreement was unfair to Nantahala.

The Commission's examination of the intercorporate agreements was undertaken in an effort to determine whether Nantahala and Tapoco function as a single, integrated electric system under North Carolina law and to determine what portion of the costs incurred by the "rolled-together" system under those contracts went to providing intrastate retail service to Nantahala's jurisdictional customers. Because the Commission determined that Nantahala incurred costs under the NFA and 1971 Apportionment Agreement that were, in effect, not required to serve its public customers and that it suffered substantial detriments thereunder, it declined to base Nantahala's demand and energy cost factors on the quantity and design of NFA entitlements Nantahala receives under the 1971 Apportionment Agreement.

The Commission, *in setting retail rates*, is no more bound to blindly apply specific rate schedules filed with and accepted by FERC, than is the FERC *in setting wholesale rates*—as opposed to *regulating* those specified rate schedules. The fact that the Commission chose a different rate making methodology than FERC to alleviate perceived inequities to Nantahala's retail customers and in so doing effectively allocated a greater proportion of system-wide costs to Alcoa (Tapoco) does not constitute a basis for rejecting the Commission's methods. State public service commissions need not follow FERC wholesale rate making methodologies; North Carolina regulatory policy, based upon factors appropriate to local utility regulation, may differ from FERC policy without necessarily coming into conflict with it. *See Public Systems v. FERC*, 709 F. 2d 73, 84 (D.C. Cir. 1983).

In view of these factors, and in light of our foregoing discussion of the respective spheres of federal and state rate making authority, we completely reject the various arguments presented by Alcoa and Nantahala on the question of federal preemption. These arguments are based, *inter alia*, upon the twin faulty premises that FERC has actually and directly approved the allocation scheme set up in the 1971 Apportionment Agreement and that the Commission's roll-in methodology impermissibly alters the costs associated with that contract and allocated to Nantahala. We have carefully examined the evidence of record, the actual mechanics of the roll-in and cost allocation performed by the Commission, and the relevant authorities on the question of federal preemption and conclude that the Commission has not crossed over the "bright line" between state and federal regulatory jurisdiction and intruded upon the federal domain, either directly or indirectly, in fixing Nantahala's retail rates in this proceeding.

B.

[18] The companies also argue that the Commission's order grants an unconstitutional preference to Nantahala's North Carolina customers over Tapoco's Tennessee customer (Alcoa) and impermissibly shifts the economic benefit of Tapoco power to Nantahala in violation of the limitation on state power implicit in the Commerce Clause of the United States Constitution (art. I, § 8, cl. 3) under the Supreme Court's decision in the *NEPCO* case, *New England Power Co. v. New Hampshire*, 455 U.S. 331, 71 L.Ed. 2d 188. We agree with the companies' contention that *NEPCO* establishes that a state utilities commission may not grant its citizens a preferred right to the benefit of hydroelectric energy generated by a utility in that state solely to gain an economic advantage over the utility's out-of-state customers, and that the granting of such a preferred benefit, regardless of how it is effectuated, places a direct and substantial burden on interstate commerce in violation of the Commerce Clause. However, we do not agree that the rule announced in *NEPCO* invalidates the action of the Commission in this case.

In *NEPCO*, hydroelectric power was produced in New Hampshire by the New England Power Company (NEPCO) and transferred to an out-of-state consortium of companies which served

six states and operated a power pool which included NEPCO. NEPCO then bought power from the pool, based on its pro rata share of the total average cost of power in the pool. This arrangement appreciably increased NEPCO's intrastate costs of service because its own hydro-generated power is cheaper to produce than most of the other generating sources in the consortium. The New Hampshire Commission, acting pursuant to a specific New Hampshire statute, terminated NEPCO's right to export its hydroelectric energy, and ordered the company to make arrangements to sell the previously exported hydroelectric energy to customers within the state. As the Supreme Court noted, although the precise contours of the New Hampshire commission's order were unclear in that it did not require the physical severance of NEPCO's connections with the power pool, it appeared to require NEPCO to sell electricity to New Hampshire utilities at special rates adjusted to reflect the savings attributable to the exclusive use of low-cost hydroelectric generation. *New England Power Co.*, 455 U.S. at 336, 71 L.Ed. 2d at 193. The commission's staff economist proposed that NEPCO effectuate the ban by allocating the economic benefit of the low-cost hydroelectric power to New Hampshire customers through "billing mechanisms" which would reserve the savings resulting from hydroelectric generation exclusively for in-state customers. *See id.* at n. 3.

On appeal, the Supreme Court of New Hampshire rejected the arguments of NEPCO and its out-of-state customers that the order was preempted by Parts I and II of the Federal Power Act and that it imposed impermissible burdens on interstate commerce. The United States Supreme Court reversed, holding that the New Hampshire commission's order attempted to restrict the flow of privately owned and produced electricity in interstate commerce in a manner inconsistent with the Commerce Clause of the United States Constitution (art. I, § 8, cl. 3) and that Section 201(b) of the Federal Power Act, 16 U.S.C. § 824(b) (the "savings clause") does not provide an affirmative grant of authority to the state to do so.

In rejecting the New Hampshire court's ruling, the Supreme Court explained its prior decisions under the implied limitation on state power in the Commerce Clause.

> Our cases have consistently held that the Commerce Clause of the Constitution, Art. I, Sec. 8, cl. 3, precludes a state from mandating that its residents be given a preferred right of access, over out-of-state consumers, to natural resources located within its borders or to the products derived therefrom. (Citations omitted.) Only recently, . . . we reiterated that "[t]hese cases stand for the basic principle that a 'State is without power to prevent privately owned articles of trade from being shipped and sold in interstate commerce on the ground that they are required to satisfy local demands or because they are needed by the people of the State'." (Citations omitted.)

New England Power Co., 455 U.S. at 338, 71 L.Ed. 2d at 194-95. Applying this anti-protectionist rule to the actions of the New Hampshire commission, the Court, with little trouble, concluded:

> The order of the New Hampshire Commission, prohibiting New England Power from selling its hydroelectric energy outside the State of New Hampshire, is precisely the sort of protectionist regulation that the Commerce Clause declares off-limits to the states. The Commission has made clear that its order is designed to gain an economic advantage for New Hampshire citizens at the expense of New England Power's customers in neighboring states. Moreover, it cannot be disputed that the Commission's "exportation ban" places direct and substantial burdens on transactions in interstate commerce. . . . Such state-imposed burdens cannot be squared with the Commerce Clause when they serve only to advance "simple economic protectionism." . . . (Citations omitted.)

Id. at 339, 71 L.Ed. 2d at 195. Thus, in *NEPCO*, the Supreme Court held invalid not only a state utility commission order that prohibits that export of hydroelectric generation from one state to another, but also an order which *exclusively* reserves to the citizens of the producing state the full economic benefit of such hydroelectric power.

However, unlike the action of the New Hampshire commission, the roll-in performed by the Commission in this case does not purport to prohibit the exportation of energy produced within North Carolina, nor does it divert the flow of Tapoco's power to

Nantahala. More importantly, the roll-in methodology used by the Commission does not exclusively reserve to the citizens of North Carolina the entire economic benefit of the unified system's low-cost in-state hydroelectric generation.

As we have stated, the purpose of the roll-in employed by the Commission was the determination of the costs of service for the combined Nantahala-Tapoco system and the allocation of those costs as between the intrastate retail customers in North Carolina and the out-of-state industrial customer (Alcoa) in Tennessee. The practice of rolling-together accounting data and allocating costs between jurisdictional and non-jurisdictional service is common throughout the United States and is no different than the rate making techniques employed by the Commission in setting intrastate retail rates for other companies, such as Duke Power or Carolina Power & Light, which serve customers in more than one state. *Cf. Colorado Interstate Gas Co. v. FPC*, 324 U.S. 581, 89 L.Ed. 1206; *Central Kansas Power Co. v. State Corporation Commission*, 221 Kan. 505, 561 P. 2d 779. The roll-in merely assures that Nantahala's in-state retail customers are not overcharged in order to subsidize a non-jurisdictional customer and that their rates accurately reflect the costs of facilities used in serving their demands upon the system.

In contrast to the action taken by the New Hampshire commission, the North Carolina Utilities Commission accepted the continuation and operation of all existing power supply agreements between and among the companies and TVA, and addressed neither the dispatch or transmission of electricity nor the actual division of energy and demand entitlements between Nantahala and Tapoco. Both Nantahala and Tapoco continued to deliver the output of their generating facilities to TVA and to receive power in exchange for resale. Under the order, Tapoco continues to deliver its return power to Alcoa and Nantahala continues to sell its share to its intrastate customers.

To support their analysis that the roll-in methodology used by the Commission constitutes an undue burden on interstate commerce under the *NEPCO* decision, the companies rely almost exclusively on one statement contained in the fifty-seven page order of the Commission. The statement is to the effect that the intervenors' proposed allocation methodology (later adopted by

the Commission), *assumed* that the North Carolina public load had a "first call on the total electric energy output of the combined Nantahala-Tapoco system." The companies essentially contend that this statement shows that the Commission was engaging in the same sort of admittedly protectionist behavior as the New Hampshire commission in *NEPCO*.

Although the argument has a certain surface appeal, it fails upon closer examination. Here, the Commission characterized the allocation methodology as premised upon a "first call" concept at the very outset of its discussion of the relative merits of the respective jurisdictional cost allocation methodologies proposed by the intervenors and the companies. However, the Commission went on to devote approximately thirty pages of its order to an analysis of (1) how the power supply agreements, *inter alia*, limited and rearranged the combined system's "demand" and "energy" availability to the detriment of Nantahala and corresponding benefit to Alcoa; (2) the various ways in which the companies' use of the apportionment of NFA demand and energy entitlements as a basis for the allocation of demand and energy costs would result in Nantahala's retail customers bearing costs properly allocable to Alcoa's use of Nantahala's resources; and (3) the preferable features of the intervenors' cost allocation methodology, which is based upon actual system capability and actual jurisdictional load responsibility for costs associated with supplying the system's entire load. The allocation factors ultimately used by the Commission do not allocate capacity and energy *availability* or *usage* between the combined system's jurisdictional and non-jurisdictional customers, but rather allocate "demand" and "energy" *costs* between the respective loads.

Alcoa concedes that no "dollar costs" incurred by Nantahala under the NFA and 1971 Apportionment Agreement are eliminated by the Commission's roll-in, but argues that the roll-in favors Nantahala's North Carolina customers by relieving them of all costs that TVA "charges" for the Fontana exchange and shifting those costs to the Tennessee load of Alcoa by means of the jurisdictional cost allocation methodology. Under the companies' proposed allocation formula, Nantahala would be assigned a percentage of demand and energy related costs based upon the demand and energy entitlements it receives under the power supply contracts. This percentage was somewhat higher than the per-

centage of costs developed by the Commission on the basis of demand and energy costs related to actual system capability and customer load demand under the intervenors' allocation methodology. Accordingly, Alcoa argues that in assigning Nantahala a "lower" percentage of costs than Nantahala "incurs" under the contracts, the Commission granted a preference for the in-state customers over the out-of-state customer.

Obviously, Alcoa's argument completely ignores the findings of the Commission that Alcoa had traded benefits usable and required by Nantahala for its public load in return for entitlements mainly usable and required by Alcoa's aluminum operations and so had already gained substantial benefits at the expense of Nantahala's public customers. Contrary to the assertions of Alcoa, intra-system retail costs of service were not allocated by the NFA and 1971 Apportionment Agreement and therefore the Commission was not bound to use the demand and energy entitlements in computing Nantahala's demand and energy related costs. The roll-in did not relieve Nantahala of all costs associated with the Fontana exchange in contravention of federal authority over those contracts, it merely determined which portion of those costs Nantahala was entitled to recoup by means of charges to its retail customers.

Despite the Commission's initial characterization, the rates actually set for Nantahala do no more than reflect the proportion of system costs of service fairly attributable to the provision of intrastate retail service. Nowhere does the Commission's discussion or application of the roll-in methodology actually implement a "first call" concept. The Commission has not granted North Carolina customers a preference to the economic benefits of hydroelectric energy generated in North Carolina at the expense of Alcoa in Tennessee, it merely eliminated from Nantahala's existing rate structure preferences and inequities which were effectuated in the past by basing Nantahala's rates on the fiction that it was a stand-alone company. This traditional exercise of its rate making authority is simply not proscribed by the rule established in *NEPCO*, or in other commerce clause cases.

It is well-settled in modern commerce clause jurisprudence that the existence of a commerce clause violation depends, in any case, upon "the nature of the state regulation involved, the objec-

tive of the state, and the effect of the regulation upon the national interest in the commerce." *Illinois Natural Gas Co. v. Central Illinois Pub. Serv. Co.*, 314 U.S. 498, 505, 86 L.Ed. 371, 376. The Supreme Court recently reformulated the basic test to be applied as follows:

> Where [a] statute regulates evenhandedly to effectuate a legitimate local public interest, and its effects on interstate commerce are only incidental, it will be upheld unless the burden imposed on such commerce is clearly excessive in relation to the putative local benefits. (Citation omitted.) If a legitimate local purpose is found, then the question becomes one of degree. And the extent of the burden that will be tolerated will of course depend on the nature of the local interest involved, and on whether it could be promoted as well with a lesser impact on interstate activities.

Pike v. Bruce Church, 397 U.S. 137, 142, 25 L.Ed. 2d 174, 178 (1970).

In *Arkansas Elec. Coop. Corp. v. Arkansas Public Serv. Comm'n*, 461 U.S. 375, 76 L.Ed. 2d 1, the Court applied the *Bruce Church* test to the question of whether state public service commission *regulation* of wholesale electric rates charged by a rural power cooperative to its member retail distributors was forbidden by the Commerce Clause of the United States Constitution. The Court upheld such "even-handed" regulation, reasoning that (1) economic protectionism is not implicated by the traditional rate making functions of the state public service commissions;[22] (2) state regulation of wholesale rates charged by a rural power cooperative is well within the scope of "legitimate local public interest," particularly where the cooperative's basic operation consists of supplying power from generating facilities located within the state to member cooperatives, despite the fact that the cooperative is also tied into an interstate power grid; and (3) the effects on interstate commerce of state regulation of wholesale rates the cooperative charges its members are only incidental, so

22. *See also Kansas-Nebraska Natural Gas Co. v. City of St. Edward*, 234 F. 2d 436, 440 (8th Cir. 1953); *Zucker v. Bell Tel. Co. of Penn.*, 37 F. Supp. 748, 757 (E.D. Pa. 1974), *aff'd*, 510 F. 2d 971, *cert. denied*, 422 U.S. 1027, 45 L.Ed. 2d 684 (1975).

that the burden imposed on such commerce is not clearly excessive in relation to the putative local benefits.

In passing, the *Arkansas Electric* Court observed that despite the fact that most retail utilities receive a portion of the power they sell from out-of-state,

> [T]he national fabric does not seem to have been seriously disturbed by leaving regulation of retail utility rates largely to the States. Similarly, it is true that regulation of the prices AECC [the cooperative] charges to its members may have some effect on the price structure of the interstate grid of which AECC is a part. But, again, we find it difficult to distinguish AECC in this respect from most relatively large utilities which sell power both directly to the public and to other utilities.

461 U.S. at 395, 76 L.Ed. 2d at 17. Thus, it is clear that in the ordinary case, and absent acts of pure economic protectionism, state regulatory action affecting both jurisdictional and nonjurisdictional customers that imposes only incidental effects upon interstate commerce will not be found to offend the Commerce Clause of the United States Constitution.

Again, the roll-in, as employed by the Commission, does no more than establish the overall cost of operation of a single, unified Nantahala-Tapoco system and allocates the proper portion of those costs to North Carolina retail customers for the purpose of fixing just and reasonable rates for Nantahala. Such evenhanded and traditional rate making operations do not implicate the national concern with "economic protectionism" discussed in the *Bruce Church* case. Moreover, the setting of retail electric rates for Nantahala's customers is clearly a legitimate North Carolina interest with a significant impact in this state. Not a word of the contracts or agreements properly regulated by FERC has been changed, and the fact that the price charged by Nantahala to its retail customers may have some *de minimis*, incidental effect on the price structure of the interstate "grid" of which Nantahala is a part is not clearly excessive in relation to the substantial public interest in the establishment of just and reasonable electric rates for ultimate North Carolina consumers. *See Arkansas Elec. Coop. Corp. v. Arkansas Public Serv. Comm'n*, 461 U.S. 375, 76 L.Ed. 2d 1. Accordingly, we conclude that the Commission's order does not

impose an undue burden on interstate commerce and is not, therefore, prohibited by the Commerce Clause of the United States Constitution.

We take this opportunity to note that an amicus curiae brief has been submitted in this appeal on behalf of the State of Tennessee and one of its agencies, the Tennessee Department of Economic and Community Development. The State of Tennessee is concerned that any increase in power costs at Alcoa's Tennessee facilities resulting from the Commission's order will create the danger of Alcoa's curtailment of production, with consequent layoffs of many local residents there. The State joins in the position of the companies (Alcoa, Tapoco) that the Commission's order interferes with FERC's exclusive jurisdiction to regulate the way in which energy is allocated and sold in interstate commerce and in the companies' argument that the roll-in order has the practical effect of allocating the power output and the economic benefit of Tapoco's operations to Nantahala in contravention of both federal authority and the federal constitution. The legal issues adverted to in the amicus brief are, of course, addressed in our discussion of the arguments presented by the companies themselves. We are fully cognizant of the broader concerns expressed by the State of Tennessee, however, we find no impermissible preferences or reallocation of resources to be embodied in the Commission's order. Rather, we conclude that the order grants precisely the relief which the State of Tennessee requests in its brief, that is, the order "ensure[s] all affected persons and entities of fair treatment in the allocation of power resources."

C.

Both Nantahala and Alcoa challenge the rate reduction and refund obligation imposed by the Commission for the locked-in period of this docket (1977-1981). Nantahala argues that implementation of the roll-in methodology causes it to suffer a revenue shortfall which affects its financial stability and amounts to confiscation of its properties in violation of the Due Process Clause of the Fourteenth Amendment to the United States Constitution and art. I, § 19 of the North Carolina Constitution (the "law of the land" provision). Alcoa attacks both the Commission's authority to impose liability upon it for Nantahala's refund obligation and the results of that imposition as confiscatory under the federal con-

stitution. We find no merit in any of the companies' arguments concerning the rate reduction or refund obligation.

1.

As indicated in Part I of this opinion, Nantahala initiated this proceeding in 1976 to establish new rates based upon the 1975 test year data so as to increase its charges to North Carolina retail customers by $1,830,791. On 14 June 1977, the Commission issued an order in Docket No. E-13, Sub 29, permitting Nantahala to put into effect revised rates so as to produce $1,598,918 in additional gross revenues. This rate increase was based upon the assumption, later and properly rejected by the Commission, that Nantahala was a stand-alone company, that its stand-alone reasonable expenses, including interest on its outstanding debt, were $9,827,514, and that its stand-alone authorized gross revenues were $11,067,000. Under the roll-in methodology used in the remanded proceedings, Docket No. E-13, Sub 29 (Remanded), Nantahala is authorized, through its rates, to collect revenues in the amount of $9,032,000 (exclusive of purchased power costs), while Nantahala's rolled-in reasonable expenses are determined to be $8,322,000. The refund imposed of $2,035,000 annually, was based upon the difference between the revenues being collected under the 14 June 1977 order in the amount of $11,067,000 and the revenues authorized in the 2 September 1981 order in the amount of $9,032,000. In other words, the refund obligation is the difference in amount between Nantahala's actual rate collections between June 1977 and August 1981, and what those collections would have been under the rolled-in rates, plus interest.

a.

[19] Nantahala contends that the roll-in sets revenues for the utility which are below its "actual" or "book" expenses and thus requires it to operate at a loss. The company arrives at its revenue shortfall conclusion by subtracting its rolled-in authorized revenues from the expenses authorized in the 1977 order on the premise that Nantahala was a stand-alone company. That is, by subtracting the $9,032,000 in gross revenues authorized under the roll-in from the $9,827,514 in reasonable expenses determined for the 1975 test year on the stand-alone premise, Nantahala arrives at an approximate $800,000 "revenue shortfall." Nantahala uses the same methodology in comparing rolled-in authorized revenues

to stand-alone authorized revenues under the 1977 order in support of its argument that the approximately $2 million annual reduction in revenues from the previously established level will deplete the utility of earnings with which to pay an equity return to its shareholder or to furnish capital for plant expansions and new service connections as its load grows. It is Nantahala's contention that the Commission, on remand, did not determine that the expenses it had earlier found reasonable would not actually be incurred by Nantahala, or that the losses thus engendered would be ameliorated by the roll-in, and that the ultimate result of the roll-in will be Nantahala's financial insolvency.

The obvious flaw in Nantahala's "revenue shortfall" argument lies in the company's failure to compare authorized rolled-in revenues to authorized rolled-in expenses. In the order appealed from, Finding of Fact No. 17 authorizes Nantahala, through its rates, to collect revenues in the amount of $9,032,000 (exclusive of purchase power costs) while Finding of Fact No. 14 recognizes Nantahala's reasonable expenses to be $8,322,000. The difference between the two figures represents profit. Consequently, Nantahala is permitted to earn a proper income over and above the rolled-in expenses that the Commission has determined were reasonably incurred in the provision of service to Nantahala's retail customers.

The fact that Nantahala claims it *actually* has incurred a higher level of expenses under the various inter-corporate agreements between itself, its affiliates and TVA is not dispositive; it is for the Commission, and not the company, to determine what portion of those total expenses are to be reflected in the retail rates charged Nantahala's North Carolina customers. It must be remembered that this is a general rate case, and that under N.C. G.S. Chapter 62, the Commission must fix such rates "as shall be fair to both the public utility and to the consumer." N.C.G.S. § 62-133(a). While the Commission is to fix rates that will enable the utility *by sound management* to pay all of its costs of operation and have left a fair return upon the fair value of its properties, it is not required to guarantee the return requested by the utility where the facts and circumstances warrant otherwise. *Utilities Comm. v. Telephone Co.*, 285 N.C. 671, 208 S.E. 2d 681. As noted earlier, the primary purpose of Chapter 62 is to assure the public of adequate service at a reasonable charge; the provi-

sions of this chapter of the General Statutes designed to assure the utility of adequate revenues do not take precedence over, but "are in the nature of corollaries to the basic proposition that the public is entitled to adequate service at reasonable rates. . . ." *Id.* at 680, 208 S.E. 2d at 687. Furthermore, as this Court noted in *Utilities Comm. v. Telephone Co.*, the question of whether rates prescribed under Chapter 62 are so unreasonable and unjust to the company and its stockholders, and so amount to an unconstitutional confiscation of a utility's property necessarily "involves an inquiry as to what is reasonable and just for the public. . . . The public cannot properly be subject to unreasonable rates in order simply that stockholders may earn dividends." 285 N.C. at 682, 208 S.E. 2d at 688, *quoting Covington & Lexington Turnpike Road Co. v. Sandford*, 164 U.S. 578, 596-97, 41 L.Ed. 560, 566 (1896).

Having found that Nantahala's parent/customer Alcoa had already received substantial concealed benefits at the expense of Nantahala's retail rate payers under the NFA and 1971 Apportionment Agreement, the Commission was entitled to weigh that benefit in balancing the interests of Nantahala's rate payers and the utility's sole shareholder, Alcoa. In view of the Commission's determination that unsound or "absentee" management decisions on the part of Nantahala, and parental domination on the part of Alcoa, left the utility with insufficient resources to meet its steadily increasing public load and lacking in contractual power supply arrangements tailored to meet its public service needs at reasonable prices, it was well within the Commission's rate making authority to shift the onus of those managerial shortcomings from the pockets of Nantahala's retail rate payers to the corporate offices of the "Alcoa power system." In short, we reject Nantahala's arguments that the rolled-in rates cause it to operate at a loss and in so doing confiscates its property.

b.

In essence, the Commission set Nantahala's rates and ordered refunds so as to return to Nantahala's retail customers the benefits which the Commission found had been unfairly diverted to Alcoa by means of Alcoa's domination of Nantahala. The principal amount of the refund obligation imposed on Nantahala is $18,962,000. By December 1983, that figure had grown to

$25,568,433. Nantahala's entire net worth as of 31 December 1983 was $15,700,000. Thus, the full extent of the costs unfairly imposed upon Nantahala's rate payers under the 1977 order was substantially greater than Nantahala itself could afford to return; the economic benefits in question had already been flowed-through to Alcoa. Therefore, to prevent the frustration of its ability to effectively protect Nantahala's customers, the Commission ordered Alcoa, over whom the Commission had previously asserted jurisdiction as a statutory public utility pursuant to N.C. G.S. § 62-3(23)c, to pay Nantahala's refund obligations to the extent that Nantahala itself is unable to do so and continue to render adequate service. Thus, Nantahala is not left bereft of resources with which to meet its obligations.

Nantahala, however, contends that its *potential* refund obligation coupled with the rate reduction prevented the utility from attracting either debt or equity financing which will be needed to meet both its service obligation and its anticipated need to expand its facilities as growth in demand on its system occurs. Nantahala observes that the Commission's order places the refund obligation on Nantahala whether or not Alcoa can be forced to contribute, so that if Alcoa is determined not to be liable for these refunds, Nantahala will be obligated to refund the entire amount. The utility implies in its brief that this situation has placed a "chill" on its credit rating. In addition, Nantahala points out that Alcoa contends that it bears no refund liability and has stated that it will make payments, "only after exhaustion of all federal and state judicial remedies and legal rights." On this basis, Nantahala argues that the requirement that it make refund payments to customers far in excess of its net worth or what it could obtain in complete liquidation of its assets also results in an unconstitutional confiscation of its property. Because Nantahala's argument concerning the refund obligation turns upon the determination of Alcoa's refund liability, we will now address the challenges Alcoa presents to the Commission's order holding it responsible for so much of the refund obligation as Nantahala is itself unable to pay.

2.

Alcoa has abandoned its argument that it is not a statutory public utility under N.C.G.S. § 62-3(23)c, as found by the Commis-

sion and affirmed by the Court of Appeals. However, the company now argues that the Commission lacks the authority to impose any refund obligation upon Alcoa on this basis and, in any event, lacks the authority to charge Alcoa with the obligation to refund any revenues collected by Nantahala prior to 3 October 1980, the date on which the Commission ruled that Alcoa was a statutory public utility. We conclude that the Commission acted well within its regulatory authority in imposing the obligation upon Alcoa to pay any part of the refund obligation for the entire locked-in period of this docket that Nantahala is itself unable to pay.

Alcoa's challenge to the Commission's basic authority to order it to pay any portion of Nantahala's refund obligation may be summarized as follows: (A) Alcoa's status as a public utility under N.C.G.S. § 62-3(23)c does not, in itself, give the Commission a basis for imposing liability on it for Nantahala's refund; (B) there is no legal or factual basis for the Commission to reach that result by either "piercing the corporate veil" between Alcoa and Nantahala or by applying the "no profits to affiliates" rule; and (C) federal regulation of the companies and transactions at issue prohibits piercing of the corporate veil. None of these contentions has any merit.

a.

[20] Initially, we note that in a general rate case, the Commission is empowered to fix rates for *any* public utility subject to the provisions of Chapter 62. Ordering refunds is an inherent part of the rate making function of the Commission. *See Utilities Comm. v. Edmisten, Atty. General*, 291 N.C. 451, 232 S.E. 2d 184 (refunds to customers ordered to remedy excessive utility charges arising out of improperly approved fuel cost adjustments in retail rates). Moreover, pursuant to N.C.G.S. § 62-30, the Commission is vested with broad authority to insure the effective regulation of public utilities in North Carolina, including "all such . . . powers and duties as may be necessary or incident to the proper discharge of its duties."

N.C.G.S. § 62-3(23)c denominates the parent of a public utility to be, itself, a public utility to the extent "that such affiliation has an effect on the rates or service of such public utility." Alcoa first argues that this statutory provision is "merely jurisdictional" and permits the Commission to "assert" its regulatory authority over

the parent corporation, but fails to provide a basis for remedial action should the affiliation be found to have a detrimental effect on the subsidiary. Next, Alcoa maintains that no other provision of the General Statutes gives the Commission such remedial jurisdiction over a statutory public utility, so that the Commission lacked a legal basis for holding Alcoa liable for Nantahala's refund obligation. We disagree.

Under Alcoa's interpretation of N.C.G.S. § 62-3(23)c it is difficult to conceive of what the "assertion" of such an empty regulatory authority would consist of. The very language of this provision indicates that it must have been the purpose of the legislature to empower the Commission to hold the corporate parent or affiliate of a public utility financially accountable for any adverse effects of that affiliation on the subsidiary's rates or service as a necessary adjunct to the discharge of its statutory duties under N.C.G.S. § 62-30. Furthermore, Alcoa's reading of N.C.G.S. § 62-3(23)c is wholly at odds with the general powers and duties granted the Commission under Chapter 62 of the General Statutes.[23]

It is beyond dispute that Nantahala's financial stability and hence its ability to serve the public depends on Alcoa's ultimate legal responsibility to stand behind the refund obligation. The broad grants of authority to the Commission to ensure the effective regulation of Nantahala and the full protection of Nantahala's customers would be rendered nugatory if, upon a finding that its parent's affiliation had severely and detrimentally affected Nantahala's rates and ability to effectively provide service in its franchise area, the Commission were powerless to order remedial action against the parent corporation. Therefore, we reject Alcoa's restrictive interpretation of the purpose of N.C.G.S. § 62-3(23)c and the scope of the Commission's statutory powers.

23. For example, N.C.G.S. § 62-42(a)(5) authorizes the Commission to enter orders directing a public utility to do ". . . any other act necessary to secure reasonably adequate service or facilities and reasonably and adequately to serve the public convenience and necessity. . . ;" subsection (b) permits an order to be directed to "two or more public utilities," and N.C.G.S. § 62-32 authorizes the compelling of a public utility to render reasonable service at reasonable rates.

b.

The provision of electric service, and the development of the hydroelectric resources of North Carolina, are enterprises in which the public has a special interest, and which are accordingly subject to special duties and regulation. N.C.G.S. § 62-2; *Public Service Co. v. Power Co.*, 179 N.C. 18, 101 S.E. 2d 593 (1919); *North Carolina Public Service Co. v. Southern Power Co.*, 282 F. 837 (4th Cir. 1922), *cert. denied*, 263 U.S. 508, 68 L.Ed. 413 (1924). When a public utility is affiliated with other corporations, it is often necessary to look beyond corporate form to determine the actual scope of the public service enterprise in question, in order to prevent evasion of the obligations imposed on that public service enterprise. *See generally* Berle, *The Theory of Enterprise Entity*, 47 Col. L. Rev. 343, 343-45, 348-52 (1947). This Court has repeatedly recognized the propriety of "piercing the corporate veil" in the context of utility regulation. In *Utilities Comm. v. Morgan, Attorney General*, 277 N.C. 255, 177 S.E. 2d 405 (1970), *aff'd on rehearing on other grounds*, 278 N.C. 235, 179 S.E. 2d 419 (1971), Justice Lake, writing for the Court, stated:

> It is well established that the doctrine of the corporate entity may not be used as a means for defeating the public interest and circumventing public policy. . . . In order to prevent such a result, a parent corporation and its wholly-owned subsidiaries may be treated as one. (Citations omitted.)

277 N.C. at 272, 177 S.E. 2d at 416. *Accord Utilities Commission v. Intervenor Residents*, 305 N.C. 62, 286 S.E. 2d 770; *Utilities Comm. v. Telephone Co.*, 281 N.C. 318, 189 S.E. 2d 705.[24] *See generally* 64 Am. Jur. 2d, Public Utilities, § 202 (1972); 16 A.L.R. 4th 454, § 4. Indeed, the inherent authority of the Commission to

24. In the *Morgan, Intervenor Residents* and *Telephone Company* cases this Court has recognized that the Commission should closely scrutinize transactions between a public utility and an *unregulated* affiliate, in order to prevent either the utility enterprise from effectively earning a greater profit than the Commission had determined to be reasonable, or from concealing or diverting profits from the public utility to the affiliate. Surely the Commission has no less authority to regulate the results of transactions between a jurisdictional or statutory public utility and its affiliated operating public utility than it has to regulate transactions between an unregulated affiliate and a public utility. We therefore reject, in passing, Alcoa's argument that the Commission could not also rely on the "no profits to affiliates" rule to hold it liable for Nantahala's refund obligation.

pierce the corporate veil between a public utility and its parent corporation in order to prevent the evasion of effective regulation was implicitly recognized in an early commercial rate discrimination case involving Nantahala and its parent/customer Alcoa. *Utilities Commission v. Mead Corp.*, 238 N.C. 451, 78 S.E. 2d 290 (Barnhill, J., concurring) (Nantahala may not structure its rates so as to accord its parent Alcoa an unreasonably favorable rate).

Therefore, once the Commission determined that Alcoa was a statutory public utility under N.C.G.S. § 62-3(23)c, it could rely upon the doctrine of "piercing the corporate veil" between Nantahala and its parent to hold Alcoa financially responsible for Nantahala's refund obligation to the extent its affiliation had adversely affected Nantahala's rates as "necessary or incident" to the proper discharge of its regulatory duties under Chapter 62. N.C.G.S. § 62-30. Accordingly, we reject Alcoa's argument that there is no statutory or legal basis for its refund liability.

[21] Alcoa next maintains that "as a matter of law" there is no factual basis in the record before the Commission for piercing the corporate veil between it and Nantahala. Alcoa's argument may be summarized as follows: (1) North Carolina law requires a finding of corporate domination utilized by the parent to commit fraud or injustice with respect to the transaction attacked; (2) the Commission's determinations are based solely on the fact of Alcoa's 100 per cent stock ownership of Nantahala and its conclusion that the NFA and 1971 Apportionment Agreement were negotiated so as to benefit Alcoa at the expense of Nantahala's customers, thereby leaving Nantahala an "empty shell"; (3) stock ownership, without more, is no basis for piercing the corporate veil and the "empty shell" characterization cannot stand as a basis for domination or injury to the rate payer because both the NFA and 1971 Agreement "have been thoroughly regulated (and approved) by FERC"; and (4) a state commission is preempted from determining that the Nantahala-Alcoa relationship resulted in fraudulent wholesale rate schedules once these rate schedules have been determined to be reasonable by FERC. Although these contentions have a certain logical appeal, they are patently lacking in merit as a matter of both law and fact.

In its order reducing rates and imposing the refund, the Commission found as a fact that:

> Alcoa has so dominated certain transactions and agreements affecting its wholly owned subsidiary Nantahala that Nantahala has been left but an empty shell, unable to act in its own self interest, let alone in the interest of its public utility customers in North Carolina.

In the concluding portion of the Commission's extensive discussion of evidence demonstrating Alcoa's control over the design, development and operation of Nantahala from its inception, the Commission stated:

> The Commission must conclude that Alcoa has so dominated these transactions and agreements affecting its wholly owned subsidiary Nantahala that Nantahala has been left but an empty shell, unable to act in its own self interest, let alone in the interest of its public utility customers in North Carolina. Alcoa's domination of Nantahala in these transactions has resulted in Nantahala's collecting, through its base rates, excess revenue from its customers in the amount of approximately $2,035,000 a year since June 14, 1977. Moreover, this inequity is further magnified by the fact that Nantahala has collected significantly additional excess revenues through operation of its Purchased Power Adjustment Clause.

First, it is apparent that there is nothing in the Commission's order which indicates that "fraud" was either an express or implied concern of the Commission. Rather, detrimental domination forms the basis of Alcoa's refund obligation. Next, Alcoa misconceives the need to demonstrate "fraud" in order to pierce the corporate veil between affiliated companies that comprise a single enterprise, whether that enterprise be a public utility or an unregulated business concern. Although we have previously acknowledged the propriety of disregarding separate corporate identities where a parent is found to have used its subsidiary as a mere "instrumentality" for the commission of fraud upon some third party, this Court has never limited the doctrine of piercing the corporate veil to the situation of fraud alone. In *Huski-Bilt, Inc. v. Trust Co.*, 271 N.C. 662, 157 S.E. 2d 352 (1967), the very case Alcoa relies upon in its brief, we stated the three elements which must be proved under the "instrumentality rule" as follows:

(1) Control, not mere majority or complete stock control, but complete domination, not only of finances, but of policy and business practice in respect to the transaction attacked so that the corporate entity as to this transaction had at the time no separate mind, will or existence of its own; and

(2) Such *control* must have been *used by the defendant to commit fraud or wrong, to perpetrate the violation of a statutory or other positive legal duty, or a dishonest and unjust act in contravention of plaintiff's legal rights*; and

(3) The aforesaid control and breach of duty must proximately cause the injury or unjust loss complained of. (Emphasis added.)

Id. at 670-71, 157 S.E. 2d at 358, *quoting Lowendahl v. Baltimore & O. R. Co.*, 247 A.D. 144, 157, 287 N.Y.S. 62, 76, *aff'd*, 272 N.Y. 360, 6 N.E. 2d 56 (1936). Clearly, despite the fact that the second element *includes* control and domination of the subsidiary or affiliate for the commission of some "fraud," it is by no means limited thereto and in fact, expressly includes domination for the commission of some unspecified "wrong," to "perpetrate the violation of a statutory or other positive legal duty," *or* an act in "contravention" of the complainant's "legal rights."

In fact, our courts have pierced the corporate veil between two corporations, or between a corporation and its sole shareholder(s), to prevent the frustration of public policy in numerous cases where fraud was not involved. *See, e.g., Waff Brothers, Inc. v. Bank*, 289 N.C. 198, 221 S.E. 2d 273 (1976) (to prevent a judgment debtor's meritorious claim from being defeated); *Henderson v. Finance Co.*, 273 N.C. 253, 160 S.E. 2d 39 (1968) (to prevent a finance company from evading the usury laws); and *Freeman v. Development Co.*, 25 N.C. App. 56, 212 S.E. 2d 190 (1975) (to enable recovery on meritorious contract and quasi-contract claims). Most recently, this Court held that the corporate veil between affiliated corportions will be pierced to prevent the owner of a rental property to escape liability for the tortious conduct of its affiliated operating company. *Glenn v. Wagner*, 313 N.C. 450, 329 S.E. 2d 326 (1985).

Significantly, in *Glenn v. Wagner*, we *relaxed* the showing to be made by the party seeking to extend liability for corporate

obligations beyond the confines of a corporation's separate entity by holding that in certain cases involving affiliated corporations (as distinct from parent and subsidiary corporations), the domination sufficient to pierce the corporate veil need not be limited to the particular transaction attacked. Rather, the separate corporate entity would be disregarded in those cases in which one affiliated corporation is shown to be "without a separate and distinct corporate identity and is operated as a mere shell, created to perform a function for an affiliated corporation or its common shareholders" without the necessity of proving that the control was also exercised over the *particular* transaction attacked. 313 N.C. at ---, 329 S.E. 2d at 331.

In reaching this result, Chief Justice Branch, writing for the Court, emphasized the fact that the theory of liability under the instrumentality rule is essentially an equitable doctrine.

> Its purpose is to place the burden of the loss upon the party who should be responsible. Focus is upon the reality, not form, upon the operation of the corporation, and upon the defendant's relationship to that operation. It is not the presence or absence of any particular factor that is determinative. Rather, it is a combination of factors which, when taken together with an element of injustice or abuse of corporate privilege, suggest that the corporate entity attacked had "no separate mind, will or existence of its own" and was therefore the "mere instrumentality or tool" of the dominant corporation.

Id. at ---, 329 S.E. 2d at 332. *Glenn v. Wagner* merely reiterated our earlier rule permitting the corporate veil between a parent and subsidiary corporation to be pierced where the parent has dominated the subsidiary and the subsidiary is "a shield for [the parent's] activities in violation of the declared public policy or statute of the State, *or* for the purpose of fraud. . . ." *Waff Brothers*, 289 N.C. at 210, 221 S.E. 2d at 280. (Emphasis added.)

Moreover, even if Alcoa were correct as to the other elements necessary to pierce the corporate veil under North Carolina law, the evidence supporting the Commission's imposition or refund liability upon Alcoa more than met the most restrictive of the various tests for inter-corporate liability—the so-called "*Lowendahl*" test—as articulated in *Huski-Bilt* and *Ac-*

ceptance Corp. v. Spencer, 268 N.C. 1, 149 S.E. 2d 570 (1966). As we indicated in Part I, C, 3 of this opinion, there is ample evidence of record of Alcoa's financial and managerial control over Nantahala from the time of its inception up until the present day, and plenary evidence demonstrating that this control extended to the ultimate operating and accounting policies of its subsidiary.

The entire historical pattern of Nantahala's development is replete with instances of the manner in which Alcoa dominated the development, sale and operation of Nantahala's hydroelectric resources and facilities, and subordinated these resources to what Alcoa considered to be the paramount needs of its aluminum smelting and fabrication operations in Alcoa, Tennessee. For example, Nantahala added generating capacity, vastly in excess of the amounts required to service its public load, for the express purpose of meeting Alcoa's expanding production needs prior to and during the war years at mid-century. Yet, in the last thirty years, Alcoa has caused Nantahala to remain inert in terms of obtaining additional capacity, either through development of additional generating facilities or through long-term purchase power agreements with others tailored to Nantahala's particular needs, as Alcoa's electricity requirements have leveled off, despite substantial constant growth in Nantahala's public load. As we observed earlier, Alcoa's unified development of the hydroelectric resources of its public utility subsidiaries was undertaken in the paramount interest of obtaining low-cost hydroelectric power for itself. Or, as more succinctly stated by Justice Barnhill in *Utilities Commission v. Mead Corp.*, 238 N.C. at 467-68, 78 S.E. 2d at 302:

> If they [the Commission] will only cut through the form to the substance, they will find just another hydroelectric power producing agency of Alcoa, retailing just enough of its production—less than 20%—to permit it to pose as a *quasi*-public corporation with the right to use the water power resources of this State, exercise the power of eminent domain, and enjoy the other monopolistic privileges accorded a public utility while it was, in fact, created and exists primarily to serve its master which seeks and must have low-cost hydroelectric power.

Justice Barnhill's 1953 observation that historically Nantahala has been no more than "another hydroelectric power producing agency of Alcoa" was fully borne out by the evidence before the Commission in 1981, as the Commission properly so found.

Furthermore, the evidence with respect to Alcoa's complete domination of Nantahala's "policy and business practice in respect to the transaction attacked," as found by the Commission, is both direct and overwhelming.

The three basic power supply contracts affecting Nantahala's rates are the 1941 Original Fontana Agreement, the 1962 New Fontana Agreement and the 1971 Nantahala-Tapoco Apportionment Agreement. Each of these contracts was, in whole or part, in effect during the 1975 test year. Although Nantahala was not even a party to the OFA, it gave to TVA the right of control of its energy production and water storage and turned over to TVA, through Alcoa, land, constituting the site for the massive Fontana Project. In return, Alcoa received 11,000 mw of energy for 20 years and its subsidiaries received power and energy entitlements dependent upon the level of generation controlled by TVA. The Commission found that the OFA still conveys significant benefits to Alcoa. Pursuant to the NFA, to which Nantahala was a *signatory* but *not* a *negotiating party*, Nantahala and Tapoco agreed to turn over their energy production to TVA in return for 218,300 kw annual assured energy. The Commission found and concluded that the evidence clearly demonstrates that the NFA was tailored to meet Alcoa's aluminum production needs without consideration of Nantahala's public service needs in western North Carolina.

From 1963 to 1971 Nantahala received its portion of the return entitlements under the 1963 Alcoa-Nantahala Apportionment Agreement. Under that agreement, Nantahala was provided 360 million kwh minimum production, plus Nantahala's actual production in excess of that figure, and additionally. Alcoa paid to Nantahala $89,200 annually for 25,600,000 kwh of energy received from TVA for TVA's use of Nantahala's flood control and storage rights. In 1971, with Nantahala facing the need to service an increasing public load, Alcoa employee George Popovich undertook the development of an apportionment formula by which Nantahala and Tapoco would contractually share the TVA entitlement

of 218,300 kw annual assured energy. The Popovich formula was incorporated into the 1971 Agreement between Nantahala and Tapoco, with Alcoa's employee Popovich representing the interests of *both* companies at the bargaining table. Under the 1971 Agreement, Nantahala rather than retaining or even increasing its allocation, was deprived of 66 million kwh average energy production annually in comparison to its 1963 Agreement with Alcoa. Since the production allowance in the TVA return entitlements was jointly shared by Nantahala and Tapoco under the NFA, the 66 million kwh detriment to Nantahala constituted a benefit to Tapoco that was passed on to Alcoa. Furthermore, the 1971 Agreement credited Nantahala with an assigned generating capacity of 54,300 kw, whereas its actual dependable generating capacity was determined to be 81,800 kw. Since the capacity allowance in the TVA return entitlements was also jointly shared by Nantahala and Tapoco under the NFA, any capacity needs of Nantahala between its assigned and its actual capacity represented an expense to Nantahala and, thus, a saving to Tapoco that was passed on to Alcoa as a concealed benefit.

In addition, under the 1963 Agreement, Nantahala received credit for relinquishing control of its flood control and storage rights to TVA, in the form of an annual payment of $89,200 from Alcoa. Despite the fact that the NFA included in the TVA return entitlement a reimbursement by TVA for the right to operate Nantahala's projects, the 1971 Agreement gave no credit to Nantahala for that reimbursement, and thus the reimbursement represented a savings to Tapoco that was passed on to Alcoa. Although the loss of the right to control the storage and flow of water for Nantahala's facilities constituted a loss of considerable value for which Nantahala was entitled to compensation, Nantahala received neither payments nor entitlements in consideration for relinquishment of these valuable rights. Additionally, the value to Tapoco of TVA's upstream Fontana Dam, was not figured into the apportionment.

Singularly lacking in the foregoing review is any evidence of the separate mind, will or existence of Nantahala as a corporation with its own identity. The Commission properly found that Nantahala and Tapoco were designed and operated as a single system and that by virtue of the terms of the Fontana Agreements, Nantahala is effectively precluded from exercising a separate will

regarding energy production. Moreover, no Nantahala employee has yet been identified who dealt with other parties at arm's length concerning the utilization of its generating resources for supplying power for Nantahala's public service obligations. To the contrary, and as found by the Commission, "Alcoa's dominance is obviously and frequently documented in the results of various arrangements it has caused Nantahala and Tapoco to enter into."

In summary, the evidence of record shows that the Fontana Agreements and the 1971 Apportionment Agreement resulted in direct inequities to Nantahala and concealed benefits to Alcoa. The situation was further aggravated because the TVA return entitlements in the NFA were entirely designed to meet Alcoa's aluminum production needs and were not suitable for Nantahala's public service needs. Nantahala had energy production capacity and it had peaking capacity from its own generating stations, yet Nantahala gave up that energy production capacity and that peaking capacity with the result that it had to buy higher cost power from TVA to meet its peaking responsibilities and its energy production responsibilities. The totality of this evidence shows convincingly that Alcoa has controlled the policy and business practice of Nantahala's energy production through a series of contractual arrangements orchestrated by Alcoa primarily to serve its own best interests.

The evidence as to Alcoa's use of its control over Nantahala to commit the wrong, or violation of duty complained of by the intervenors was equally substantial. Fundamentally, the record shows that Nantahala continually failed to protect its rights in its dealings with Alcoa and Tapoco concerning the power supply vital to fulfilling its public service responsibilities. For example, the NFA is silent as to any interest of Nantahala in receiving an assured portion of the return entitlements given by TVA in exchange for receiving the entire output of the Nantahala-Tapoco generating resources, except to state that the rights and benefits to Alcoa may be allocated as Alcoa, Tapoco and Nantahala see fit. The silence as to Nantahala's interest is understandable only in light of the fact that during the year 1962 Nantahala had no reason to bargain at arm's length for power suited to its public service load because the attempt to sell its distribution system to Duke Power Company was pending, and had in fact received initial approval by the Commission. Alcoa's own internal documents

indicate that should the sale have not been completed by the effective date of the NFA, TVA would *temporarily* increase the power available to the Alcoa system in an amount sufficient to meet Nantahala's needs, thus implying that the NFA was itself in no manner intended to provide Nantahala with a 20 year power supply suitable for a growing public load. However, no fundamental changes in the terms of the NFA exchange were made following this Court's reversal of the prior order of the Commission approving the sale to Duke. The circumstances surrounding execution of the NFA ultimately required Nantahala to deal separately with Alcoa, outside the NFA, for recognition of its interests.

Again, this arrangement demonstrates that although Alcoa bargained with TVA concerning the value of Nantahala's generating resources as part of a unified utility system, the structure of the NFA return entitlements suited Alcoa, not Nantahala. Later, by the terms of the 1971 Apportionment Agreement, Nantahala effectively waived certain valuable contractual rights it had been accorded under the 1963 Agreement with Alcoa *and* simultaneously received a lesser share of the TVA entitlements at a precise point in time when its load was quickly outstripping its ability to serve under the terms of the NFA exchange. The 1971 Agreement represents more than a failure of consideration to Nantahala; there was diminution of past consideration in contravention of Nantahala's legal rights.

Nantahala is a public utility with a franchise to serve the electrical needs of most of six western North Carolina counties and, in the test year, served upward of 30,000 customers. In return for the various quasi-monopolistic privileges Nantahala receives as a public utility, Nantahala has a duty to serve its customers without concealment of excessive rates. *Utilities Comm. v. Telephone Co.*, 281 N.C. 318, 189 S.E. 2d 705. By virtue of the domination of Alcoa, Nantahala was found to have been passing concealed benefits on to Alcoa which has resulted in excessive rates to its customers. This constitutes unjust action by Alcoa in contravention of Nantahala's legal rights and obligations. That this domination and unjust action in contravention of Nantahala's rights and obligations proximately caused the injury and loss complained of is, therefore, self-evident.

c.

[22] Alcoa does not directly challenge the evidentiary support for the Commission's findings and conclusions. Rather, Alcoa argues that "federal regulation and approval of the New Fontana Agreement is conclusive evidence that Alcoa does not dominate or control Nantahala through that Agreement" and "also bars a determination of either fraud or injustice to Nantahala's customers." Again, the Commission did not, and need not, find "fraud" in the agreements in order to hold Alcoa responsible for the refund obligation. Therefore, we need not address Alcoa's argument that the Commission is preempted from finding fraud in FERC-approved rate schedule. *See also* Part II, A, *supra*. In essence, Alcoa's remaining arguments boil down to the proposition that extensive prior investigation and regulation of the activities of Alcoa and Nantahala by both state and federal regulatory agencies precludes the Commission as a matter of law from finding either domination or injustice in the Alcoa-Nantahala relationship.

In light of the record of Alcoa's repeated and largely successful efforts over the last 40 years to evade, avoid and preclude federal and state regulatory oversight of its subsidiaries' energy producing operations and the various intercorporate power supply agreements between and among them and TVA, we find Alcoa's argument both factually and legally insupportable.[25] Alcoa has failed to demonstrate that any aspect of federal regulatory action with respect to Nantahala and Tapoco preempts the Commission's findings and conclusions with respect to piercing the corporate veil between itself and its public utility subsidiary.[26] It must be remembered that the Commission is charged with the regulation of public service enterprises, which require special State oversight to protect consumers from abuses of their quasi-monopoly power, in order to ensure fairness to the public. N.C. G.S. § 62-2, -30. *Manufacturing Co. v. Aluminum Co.*, 207 N.C. 52, 175 S.E. 2d 698. The Commission's oversight jurisdiction with regard to Nantahala's intrastate retail rates is exclusive, and its determination that Alcoa was legally responsible for Nantahala's excessive intrastate retail rates rests well within the realm of

25. *See* Discussion Part I, B, *supra*.

26. *See* Discussion Part II, A, *supra*.

regulatory control reserved to the states under the Federal Power Act. 16 U.S.C. § 824(b).

In summary, there is ample evidence in the record of Alcoa's financial and managerial control over Nantahala from the time of its inception, and the use of that control to impose upon Nantahala contracts in Alcoa's interest rather than in the interest of Nantahala, amounting to complete domination of policy and business practice "so that the corporate entity as to [these] transaction[s] had at the time no separate mind, will or existence of its own. . . ." *Huski-Bilt*, 271 N.C. at 671, 157 S.E. 2d at 358; *Acceptance Corp.*, 268 N.C. at 9, 149 S.E. 2d at 576. Furthermore, because Alcoa's domination resulted in the sacrifice of a public utility's resources to the needs of a private industrial concern, Alcoa's control may indeed be said to have been used to commit wrong, or to perpetrate the violation of a statutory duty owed Nantahala's customers. *Id.* Finally, the aforesaid control and breach of duty may clearly be said to have proximately caused the injury complained of, *id.*, that is, higher rates for Nantahala's customers. We therefore reject Alcoa's argument that no factual or legal basis exists for the Commission to "pierce the corporate veil" between itself and Nantahala.

d.

In its final arguments concerning the refund obligation, Alcoa maintains (1) that it was "surprised" at being declared a public utility and that it cannot be required to pay refunds based upon Nantahala's overcollections prior to 30 October 1980, the date on which it "became" a public utility; and (2) that the refund obligation is confiscatory.

1.

[23] The mere statement of Alcoa's first contention reveals the underlying fallacy of the argument: Alcoa did not "become" a North Carolina statutory public utility in 1980. This date marks the advent of no new North Carolina law expanding the definition for the first time. Nor does it mark any dramatic change in Alcoa's relationship with its subsidiaries such that the designation "public utility" was *then* appropriate for the first time. Instead, 30 October 1980 merely marks that date of the Commission's determination that, based upon Alcoa's ownership of Nan-

tahala's stock (a fact existing since 1929) and on the basis of the various intercorporate transactions and agreements, dating back at least to 1941, Alcoa satisfied the criteria for public utility status under N.C.G.S. § 62-3(23)c. In essence, Alcoa was found to have been a "public utility" having an effect on Nantahala's rates and service for many years. Based upon this finding, and upon the Commission's findings of detrimental domination, Alcoa can properly be held to pay any refunds Nantahala is ordered to pay in this proceeding, but is unable to satisfy out of its own financial resources. Inasmuch as Alcoa is not asked to pay refunds attributable to any past period (that is, prior to the 1977 rate increase), the concept of retroactive rate making is not implicated by the refund obligation ordered.

2.

[24] We also reject Alcoa's argument that the result of the Commission's order is a confiscation of its property under the rule established in *FPC v. Hope Gas Co.*, 320 U.S. 591, 88 L.Ed. 333 (1944) (the fixing of just and reasonable rates involves a balancing of the investor and the consumer interests; the investor's interests include a rate of return sufficient to produce revenue for operating expenses, service on debt and stock dividends). While it is true that Nantahala has neither supplied Alcoa with power, nor paid a dividend to Alcoa since e[illegible] 1979, these facts do not render the rates established confiscatory under the circumstances of this case. The Commission's order does no more than strike a fair and reasonable balance between the long-neglected interests of Nantahala's customers and the corporate parent whose self-interest has been so long and so well served through intercorporate domination and control. Thus, we find no merit in either the arguments presented by Nantahala or Alcoa with respect to confiscation of their property.

Finally, with respect to Alcoa's liability for Nantahala's refund obligation, we must point out that Alcoa itself has repeatedly undertaken in the past to warrant or otherwise back up its subsidiaries' performance obligations. In both Fontana Agreements, Alcoa warranted that it was backing up or securing the performance of its subsidiaries (including Nantahala) in carrying out the coordination and exchange agreements with TVA. These undertakings by Alcoa certainly undercut Alcoa's intimations that

it was surprised in any manner by being held responsible for the obligations of its wholly-owned subsidiary on the basis of its parental impact upon Nantahala's rates and service.

3.

[25] Nantahala presents one final set of arguments concerning the extent of the refund obligation. First, Nantahala contends that it cannot be required to refund revenue collected prior to 6 March 1979, because this revenue was derived from rates approved by the Commission which were not subject to being refunded prior to the Court of Appeals' reversal of the Commission's approval of the 1977 rates in Docket No. E-13, Sub 29. 6 March 1979 is the filing date of the Court of Appeals decision in *Utilities Comm. v. Edmisten, Atty. General*, 40 N.C. App. 109, 252 S.E. 2d 516, *aff'd in part and rev'd in part*, 299 N.C. 432, 263 S.E. 2d 583. Next, Nantahala contends that if it is responsible for all refunds dating to June 1977; it can only be required to refund the excess of its collected revenue over the revenue allowed in its most recently approved prior rate case, which would be in Docket No. E-13, Sub 23. We find no merit in either of these contentions.

a.

Briefly, by order of the Commission dated 14 June 1977, Nantahala was authorized to put new and increased rates into effect. This order was appealed to the Court of Appeals in the aforementioned case. That court reversed and remanded the order, stating:

> The order of the Commission dated 14 June 1977 authorizing increased rates for Nantahala and approving a new purchased power cost adjustment clause is vacated and set aside.

40 N.C. App. at 119, 252 S.E. 2d at 522. The effect of that decision, if left standing, would have been to require an immediate refund of the increased rate collections as of 6 March 1979. Subsequently, this Court stated:

> The Commission's order of 14 June 1977 authorizing an increase in Nantahala's rates was vacated by the Court of Appeals. The effect of the Court of Appeals' decision was stayed, however, by this Court's issuance of a writ of supersedeas pending the outcome of this appeal. Although that writ is hereby dissolved, we believe that essential fairness to all the parties is best served by allowing the increased rates to remain in effect, conditioned upon Nantahala's guarantee that it will in the future *refund to it customers any overcharges should the new rates ultimately be determined excessive*. Accordingly, we reverse the Court of Appeals' setting aside of the order of 14 June 1977 and direct the Commission to obtain adequate assurances of Nantahala's willingness and continued ability *to refund such overcharges as may ultimately result from imposition of the 1977 rate schedule*. (Emphasis added.)

299 N.C. at 444, 263 S.E. 2d at 592.

Upon remand to the Commission, the Commission ordered Nantahala to file an undertaking to refund, stating that:

> [T]he Supreme Court has given this Commission a clear mandate to obtain adequate assurances of Nantahala's willingness and continued ability to refund such overcharges as may ultimately result from the imposition of the 1977 rate schedule. . . .

Thereupon, Nantahala filed an undertaking, wherein Nantahala agreed:

> [T]o refund in a manner to be prescribed by the Commission the amount, if any, found to be owing to its customers should the rates approved by the order of 14 June 1977 be ultimately determined to be excessive. . . .

In its 2 September 1981 Order Reducing Rates and Requiring Refund, the Commission directed Nantahala to make a full and complete refund of all overcollections charged after 14 June 1977, when the higher rates had been put into effect. This order of the Commission is no different in substance from the order to refund overcharges collected under excessive rates which are ultimately disapproved as mandated by our decision in *Utilities Comm. v. Edmisten, Atty. General*, 291 N.C. 451, 232 S.E. 2d 184. In that case, an order of the Commission permitting Duke Power Company (and also CP&L and VEPCO) to collect a surcharge was disapproved on appeal. We stated:

> [T]his matter is remanded to the Court of Appeals for the entry of a judgment by it remanding the matter to the Commis-

> sion for the entry of an order by the Commission vacating its order authorizing the surcharge and directing Duke to make the appropriate refunds to its customers on account of revenues unlawfully collected from them pursuant to the surcharge.

Id. at 474, 232 S.E. 2d at 198.

Nantahala contends that refunds may not be ordered for pre-1979 overcollections because these occurred under rates approved by the Commission on 14 June 1977 which were not subject to any undertaking to refund until 6 March 1979, when the Court of Appeals vacated the 1977 order. Nantahala, relying upon *Utilities Comm. v. City of Durham*, 282 N.C. 308, 193 S.E. 2d 95 (1972), *Utilities Comm. v. Edmisten, Atty. General*, 291 N.C. 451, 232 S.E. 2d 926 and *Utilities Comm. v. Edmisten, Attorney General*, 294 N.C. 598, 242 S.E. 2d 862 (1978), argues that only rates that were imposed unlawfully or were permitted to go into effect, subject to an undertaking to refund, may be refunded. Nantahala further contends that because the subject rates were initially approved by the Commission, they are automatically deemed "just and reasonable" under N.C.G.S. § 62-132; therefore, they cannot be considered "unlawful" for purposes of requiring a refund at a later date. This, Nantahala contends, would constitute "retroactive" rate making, in excess of the Commission's authority, because N.C.G.S. § 62-132 permits the Commission to award refunds only where rates that it *allows* to go into effect, as opposed to rates which it *approves*, are later determined to be unreasonable. Next, Nantahala argues that it did not execute an undertaking to refund regarding the 1977 rates until after 6 March 1979, so that only overcollections after that date may be refunded under the line of cases cited above.

Nantahala's argument, although not without logical appeal, confuses the issue with respect to the refund ordered in this case. As Nantahala itself observed in its brief, both *Edmisten* cases cited above discussed the authority of the Commission under N.C.G.S. § 62-132[27] to award refunds to rate payers, where a utility collects rates *different and higher than those approved by the Commission*. This statute and the cases cited by Nantahala have no applicability to the situation under discussion. Here, excessive rates, initially but erroneously approved by the Commission, were permitted to remain in effect pending the ultimate resolution of the contested factual issue concerning the appropriate rate making methodology to utilize when fixing Nantahala's retail rates. N.C.G.S. § 62-132 cannot be relied upon to transmute an excessive rate into a "just and reasonable" rate by virtue of labeling such rates as rates "established by the Commission." Therefore, the distinction recognized under that statute with respect to the need for an undertaking to refund before refunds may be ordered on the basis of revenue collected under "established" rates has absolutely no bearing on the extent of Nantahala's refund obligation.

Moreover, it is elementary that the Commission's approval of any rate is always subject to judicial review. It is equally well-settled that rates or charges fixed by an order of the Commission are to be considered just and reasonable unless and until they are changed or modified on appeal or by the further action of the Commission itself. *In re Utilities Co.*, 179 N.C. 151, 101 S.E. 619 (1919). *See also R.R. v. R.R.*, 173 N.C. 413, 92 S.E. 150 (1917). Thus, the 1977 rates were only *presumed* to have been lawfully approved by the Commission until the 1977 order was reviewed by our appellate courts. When, upon appellate review *and* further action by the Commission itself, the 1977 rates were determined to be excessive, Nantahala's rate payers became entitled to recover *all* overcharges collected pursuant thereto. The various dates upon which appellate decisions were entered in this case have ab-

27. N.C.G.S. § 62-132 provides:

The rates established under this Chapter by the Commission shall be deemed just and reasonable, and any rate charged by any public utility different from those so established shall be deemed unjust and unreasonable. Provided, however, that upon petition filed by any interested person, and a hearing thereon, if the Commission shall find the rates or charges collected to be other than the rates established by the Commission, and to be unjust, unreasonable, discriminatory or preferential, the Commission may enter an order awarding such petitioner and all other persons in the same class a sum equal to the difference between such unjust, unreasonable, discriminatory or preferential rates or charges and the rates or charges found by the Commission to be just and reasonable, nondiscriminatory and nonpreferential, to the extent that such rates or charges were collected within two years prior to the filing of such petition.

solutely no bearing upon the temporal extent of Nantahala's refund obligation.

The premise underlying such a refund obligation is that rates which are found to be excessive are then *considered* to have been illegal from the outset, and are not considered to have become illegal only as of the date on which the appellate court has found them to be so. *See Louisville & N. R. Co. v. Greenbriar Distillery Co.*, 170 Ky. 775, 187 S.W. 296 (1916). The Commission's order with respect to the temporal extent of the refund obligation is, therefore, compatible with the mandate of this Court in *Edmisten*, and well within the Commission's inherent authority to order a public utility to refund monies which were overcollected from its customers under excessive and unlawful rates. *See* N.C.G.S. §§ 62-30, -130; -132; *Utilities Comm. v. Edmisten, Atty. General*, 291 N.C. 451, 232 S.E. 2d 184.

In answer to the additional point raised by Nantahala in this regard, we hold that the concept of "retroactive rate making" has no application in the instant proceeding. The rates ultimately fixed and the refund ordered by the Commission in the Sub 29 (Remanded) proceeding were not collectible for past service, but for service rendered in the locked-in period of this docket.

b.

[26] Finally, Nantahala challenges the Commission's action in measuring the excess revenue collected by the rates set under the roll-in rather than upon any excess revenue collected over and above what would have been collected under Nantahala's prior rate schedule, established in Docket No. E-13, Sub 23. While it is true that the rates ultimately established by the Commission in the Sub 29 (Remanded) proceeding were actually lower than the rates which Nantahala had in effect prior to 14 June 1977 by virtue of its earlier rate case (Sub 23), this fact is irrelevant to the amount of excess revenues which Nantahala's customers are entitled to receive under the rates properly established in the Sub 29 (Remanded) proceeding.

The Sub 23 rates were effectively superseded by the 1977 rates. Had the Court of Appeals decision in the original appeal from the Sub 29 proceeding been permitted to stand without appeal, the effect would have been dismissal of the Sub 29 rate in-

crease request and the Sub 23 rates would, indeed, have been effectively reinstated. However, when this Court permitted the 1977 rates to remain in effect, and remanded the case for further consideration, the Sub 29 proceeding was effectively continued until such time as the Commission modified its 14 June 1977 order and reduced Nantahala's rates. At no point in time were the Sub 23 rates "resurrected." Therefore, its refund obligation may not be measured against Nantahala's earlier, superseded rates, but must be calculated on the basis of overcharges actually levied and collected from the retail rate payers during the entire 1977-1981 period.

D.

[27] Finally, both Alcoa and Nantahala challenge the Commission's order on the grounds that the Commission failed to make independent findings of fact as to the propriety of the roll-in device in fixing Nantahala's rates. The companies primarily base their argument on certain phrases contained in the Commission's 2 September 1981 order referring to statements contained in this Court's opinion in *Edmisten*, 299 N.C. 432, 263 S.E. 2d 583, as "findings." Nantahala contends that the Commission has thereby shown that it has either improperly taken this Court's observations or concerns as facts binding upon it or has chosen to disregard substantial quantities of evidence that roll-in is inappropriate and that the NFA and 1971 Apportionment Agreement do not convey hidden benefits to Alcoa. Alcoa approaches the issue somewhat differently. It contends that the remanded hearings as to its status and liability for the refund obligation was not truly "*de novo*" because the Commission accorded an improper presumption of validity to findings made in the prior Sub 29 hearing and to purported "findings" contained in our decision in *Edmisten*. Alcoa argues that the effect of this was to improperly shift the burden of proof onto Alcoa to rebut or disprove findings established in a case to which Alcoa was not then a party, in violation of Alcoa's due process right to be heard on all issues affecting it.

Although we fully agree with the Court of Appeals that the Commission's use of such phraseology is "unfortunate," we completely reject the companies' arguments that the findings actually made by the Commission on all issues addressed in the remanded

proceedings were anything less than fully independent and fully supported by substantial, if not overwhelming, evidence of record. In *Edmisten*, we remanded the matter to the Commission for the purpose of considering the propriety of treating Nantahala and Tapoco as a single utility enterprise and determining whether Nantahala's customers would benefit by application of a rolled-in rate making methodology. As we indicated in Part I, A of this opinion, our discussion of these factual issues was limited to the purposes of demonstrating the legal basis for reversal of the 1977 order—failure to accord more than minimal consideration to material facts of record bearing upon the determination of reasonable rates for Nantahala—and the legal significance of evidence indicating that Nantahala had structured its economic affairs so as to afford an unfair preference to its parent Alcoa at the detriment of its intrastate retail rate payers.

This Court in *Edmisten* did not, as it indeed could not, "find facts"; that duty is imposed solely on the Commission. N.C.G.S. § 62-94; *Utilities Comm. v. Coach Co.*, 260 N.C. 43, 132 S.E. 2d 249 (1963). In addition, the weight of the evidence presented is also for the Commission, and not the court, to decide. *Utilities Comm. v. City of Durham*, 282 N.C. 308, 193 S.E. 2d 95. Even a cursory reading of the 1981 order shows that the Commission's references to this Court's opinion are included in an evident effort to demonstrate that, upon remand, and in keeping with the directive of this Court, adequate consideration was given to the material facts of record highlighted by this Court in its opinion. Moreover, the clearest proof of the Commission's exercise of its independent judgment in gathering and weighing evidence that dealt with the roll-in question and the issue of Alcoa's liability for its subsidiary's refund lies in the extensive and detailed discussion of the Evidence and Conclusions for Findings of Fact Nos. 4, 5, 6, 7 and 21. This discussion embraces almost one-fourth of the nearly sixty page order reducing rates and ordering refund payments. It is clearly based upon the many volumes of testimony taken and scores of exhibits received upon remand, and not upon any observations of this Court.

Nantahala's argument concerning the Commission's factual findings amounts to little more than a disagreement with the *result* reached by the Commission as to whether a roll-in should be performed and which jurisdictional cost allocation methodology

would most accurately reflect the cost of service attributable to Nantahala's intrastate retail customers. Although there was evidence of record which would perhaps support the position taken by Nantahala with respect to the roll-in, that does not entitle Nantahala to a reversal of the order. The test upon appeal from a determination of the Commission is whether the Commission's findings of fact are supported by competent, material and substantial evidence in view of the entire record. N.C.G.S. § 62-94 (b)(5). Nantahala does not even attempt to argue that the challenged findings are not supported by substantial evidence and we have no difficulty in holding that they are. Nantahala merely argues that the Commission has "ignored" evidence to the contrary.

Although the Commission must consider and determine controverted questions by making findings of fact and conclusions of law, and set forth the reasons and bases therefor "upon all the material issues of fact, law, or discretion," N.C.G.S. § 62-79(a)(1), it need not comment upon every single fact or item of evidence presented by the parties. Accordingly, we find no merit in any of Nantahala's arguments concerning the findings of fact supporting the Commission's rate reduction and refund order. Rather, we conclude that the Commission, after careful consideration of all the evidence presented upon remand, adequately weighed and discussed all the material issues of fact raised thereby and properly reached its own independent decision as to the propriety of and necessity for the roll-in and the method for implementing it.

Alcoa's argument that the Commission denied it a fair hearing by relying on "fact finding" by this Court and findings made by the Commission in the Sub 29 hearing is based almost exclusively on a single paragraph in the Commission's order, which states:

> These findings by the Supreme Court, that Nantahala and Tapoco constitute a single, integrated electric system and should be treated as one system for rate-maing purpose [sic], have been carefully considered by the Commission for purposes of this proceeding. However, since Alcoa and Tapoco were not parties to the original proceeding that led to the June 14, 1977 Order, the Commission has allowed them and Nantahala to introduce evidence in the remand proceeding to challenge the findings of the Supreme Court.

Alcoa argues that the foregoing statement indicates that the Commission improperly shifted the burden of proof and that its requirement that Alcoa disprove "findings" from a prior hearing at which it was not even present influenced the Commission's ultimate determinations concerning Alcoa's liability. Alcoa reasons that had it been accorded a proper *de novo* hearing, the result could well have been different; therefore, the Commission's order should be reversed. We do not agree.

The paragraph relied upon by Alcoa in its argument follows a discussion by the Commission of certain conclusions by this Court in *Edmisten* as to the existence, sufficiency, and legal significance of evidence adduced in the Sub 29 proceeding which indicated that Nantahala and Tapoco were designed and operated as a single system and ought therefore, be treated as such for rate making purposes under a roll-in device or methodology. Immediately following the quoted paragraph is a lengthy recital of the evidence supporting the Commission's conclusion that the Nantahala and Tapoco electric facilities *do* constitute a single, integrated system, are operated as such and are coordinated as such with the TVA system, and its further conclusion that the two companies' financial data should be rolled-in for rate making purposes as this would benefit Nantahala's customers. The mere fact that the Commission's ultimate findings and conclusions regarding the roll-in are consonant with this Court's earlier discussion of certain aspects of the original evidence does not invalidate the entire Sub 29 (Remanded) proceedings or order. Nothing in the record before us indicates that the Commission improperly placed a burden on Alcoa, or otherwise denied it a fair hearing. In fact, at the remanded hearing, the Commission permitted all participants the right to present any appropriate evidence on the relevant issues and to cross-examine all witnesses. The Commission never stated that Alcoa had "failed to rebut" any presumptions or to carry any particular "burden of proof," and the evidence was more than sufficient for the Commission to have reached the conclusion that it did as to Alcoa's liability without the benefit of any presumptions or other procedural devices. Under the circumstances of this case, the Commission's unfortunate use of the phrase "findings by the Supreme Court" does not itself warrant reversal of the Commission's order.

We also reject Alcoa's argument that it did not receive a true *de novo* hearing on all issues affecting its status and liability as a statutory public utility and that this constitutes reversible error. The record reveals that upon remand, the Commission recognized the right of both Tapoco and Alcoa to be heard *de novo* on such issues as affected them and upon which they desired *de novo* consideration of evidence. Specifically, the Commission ordered:

> Tapoco and Alcoa are entitled to be heard, *de novo* on the prior record compiled in the proceeding, but only as the further consideration of such evidence affects them. Such *de novo* hearing includes cross-examination and the right to offer evidence on their own behalf which addresses matters previously addressed. Since the prior record in this case is lengthy, and since many of the issues already determined will not affect Tapoco and Alcoa, it will be incumbent upon the Respondents to specify in advance of the hearing the issues on which they desire to be heard. The Commission can appreciate that until the Intervenors and Public Staff have stated their positions, Respondents may not know on what issues they desire to be heard *de novo*. The Commission may schedule a pre-hearing conference after all direct testimony has been prefiled in order to resolve some of these problems.

During the remanded hearings, the Commission accepted various portions of the original hearing without change by any party, such as the capital structure, embedded cost of debt, proper equity, and overall rates of return established for Nantahala in the 14 June 1977 order. No party offered any evidence upon those aspects of the case. However, as to the contested issues of public utility status, the propriety of the roll-in and the jurisdictional cost allocation method to be used, all parties, including Nantahala, Alcoa and Tapoco, were permitted to present such evidence as they desired.

All three companies, Nantahala, Alcoa and Tapoco, introduced testimony and extensively cross-examined the intervenors' witnesses. At no time did the Commission deny a request by Alcoa or Tapoco to put on evidence or cross-examine witnesses from the first set of hearings with respect to particular facts. Although not expressly directed to do so by this Court, the Com-

mission in effect afforded all parties a *de novo* hearing with respect to *any issue* properly raised by them. In every material respect, the remanded proceedings were conducted as *de novo* hearings on both the jurisdictional and substantive issues involved in this case. Any matters not expressly redetermined from the original hearing were matters which were not in controversy and which were, if anything, favorable to Nantahala, and therefore, to Alcoa. Accordingly, we reject Alcoa's assertion that the "hearing below was an arbitrary and capricious drama," in which its due process right to be heard on all issues affecting it was not respected. To the contrary, we conclude that all parties received a full and fair hearing at all stages of the original and remanded proceedings and that the Commission's order was, in all respects, based upon fully independent and well substantiated findings of fact and conclusions of law.

III.

We have carefully reviewed the lengthy record compiled in this proceeding, the many and complex arguments presented by the parties and the amici curiae, and the relevant authorities cited by the parties in their briefs and those later submitted to this Court as additional authority. For the reasons stated in Parts I and II of this opinion, we conclude that the Utilities Commission has properly decided all factual and discretionary issues related to the roll-in, rate reduction and refund obligation based upon competent, relevant and substantial evidence in view of the entire record. We further conclude that the order reducing rates and requiring refunds for Nantahala's intrastate retail rate payers is free from any statutory or constitutional infirmity.

Specifically, we hold that: (1) the Commission correctly determined that Tapoco is a public utility in North Carolina, subject to its regulatory authority and jurisdiction; (2) the Commission's order has in no way contravened the terms and conditions of Tapoco's federal license to operate hydroelectric plants in North Carolina and Tennessee and the Commission is not, therefore, preempted from implementing the roll-in by virtue of Part I of the Federal Power Act and the Supremacy Clause of the United States Constitution; (3) the Commission properly determined that a roll-in for rate making purposes was mandated in the case of Nantahala and Tapoco on the grounds that (a) Nantahala has

not been designed, developed and operated as a stand-alone electric system, (b) the Nantahala and Tapoco electric facilities constitute a single integrated electric system, and (c) the two corporate affiliates should be treated as a single utility system for rate making purposes, in view of their historical development, actual operating conditions and the fact that Nantahala's customer cost responsibility cannot be accurately determined using a "stand-alone" model; (4) the Commission correctly determined that Alcoa is a North Carolina public utility under the provisions of N.C.G.S. § 62-3(23)c by virtue of the substantial and ultimately detrimental impact Alcoa's affiliation has had upon Nantahala's rates; (5) the roll-in methodology utilized by the Commission is not barred under the Supremacy Clause of the United States Constitution (a) either by virtue of Part II of the Federal Power Act or (b) by virtue of federal regulatory action in a parallel wholesale rate case; (6) utilization of the roll-in does not grant a preference to Nantahala's North Carolina customers and does not impermissibly interfere with interstate commerce in violation of the Commerce Clause of the United States Constitution; (7) application of the roll-in methodology as developed by the Commission, with its resulting reduction in retail rates and refund obligation, does not impermissibly impair Nantahala's ability to earn a proper rate of return on its investment and does not amount to a confiscation of its properties; (8) the Commission acted well within its regulatory and rate making authority in imposing the obligation upon Nantahala's parent Alcoa to pay any portion of the refund obligation for the entire locked-in period of Docket No. E-13, Sub 29 (Remanded) as Nantahala is financially unable to make; (9) prior federal and state regulation of Nantahala and Alcoa, the various transactions and the agreements affecting Nantahala's power supply does not prohibit or preempt the Commission from piercing the corporate veil between Alcoa and its wholly-owned subsidiary to hold Alcoa financially responsible for Nantahala's refund obligation; (10) the results obtained under the roll-in do not amount to a confiscation of Alcoa's property; (11) the Commission properly ordered Nantahala to refund to its North Carolina retail customers all revenue collected under the rates approved by the Commission Order issued 14 June 1977, to the extent that said rates produced revenue in excess of the level of rates approved in the Sub 29 (Remanded) proceedings and Order issued 2 September 1981; and (12) all parties received a full and fair hearing at all

stages of the original and remanded proceedings and the Commission's order is, in all respects, based upon fully independent and well substantiated findings of fact and conclusions of law.

For the foregoing reasons, the decision of the Court of Appeals upholding the Commission's order reducing Nantahala's retail rates and requiring refunds to its North Carolina retail customers is

Affirmed.

Justice VAUGHN did not participate in the consideration or decision of this case.

STATE OF NORTH CAROLINA, EX REL. UTILITIES COMMISSION	)	
v.	)	ORDER
NANTAHALA POWER AND LIGHT COMPANY; ALUMINUM COMPANY OF AMERICA; AND TAPOCO, INC.	)	

No. 227A83

(Filed 16 July 1985)

NANTAHALA Power and Light Company's (hereinafter "Nantahala") Motion for Writ of Supersedeas filed herein on 17 July 1985 is DENIED.

The orders of the North Carolina Utilities Commission, affirmed by this Court on 3 July 1985, requiring Nantahala to make refund payments to its customers are temporarily stayed to and including the 31st day of July 1985 but no longer. The temporary stay allowed by this order will expire automatically at 12:01 a.m. on 1 August 1985 without the necessity of any further order by this Court. The purpose of the stay is to permit Nantahala to seek a writ of certiorari and stay from the United States Supreme Court.

By order of the Court in Conference, this 18th day of July 1985.

MITCHELL, J.
For the Court

STATE OF NORTH CAROLINA, EX REL. UTILITIES COMMISSION

v.

NANTAHALA POWER AND LIGHT COMPANY; ALUMINUM COMPANY OF AMERICA; AND TAPOCO, INC.

ORDER

No. 227A83

(Filed 18 July 1985)

THE Aluminum Company of America's (hereinafter "Alcoa") Petition for Writ of Supersedeas filed herein on 12 July 1985 is DENIED.

The orders of the North Carolina Utilities Commission, affirmed by this Court on 3 July 1985, requiring Alcoa to assist in the making of refund payments to customers of Nantahala Power and Light Company are temporarily stayed to and including the 31st day of July 1985 but no longer. The temporary stay allowed by this order will expire automatically at 12:01 a.m. on 1 August 1985 without the necessity of any further order by this Court. The purpose of the stay is to permit Alcoa to seek a writ of certiorari and stay from the United States Supreme Court.

The stay granted herein is conditioned upon the tiling with this Court of confirmation by the Aluminum Company of America and Federal Insurance Company that the Bond (Bond No. 80965200) dated 8 February 1984 and filed in this cause on 9 February 1984 remains in full force and effect during the pendency of the stay herein granted.

By order of the Court in Conference, this 16th day of July 1985.

MITCHELL, J.
For the Court

APPENDIX B

Opinion Of The North Carolina Court of Appeals

In my opinion the dismissal by the trial court was correct and my vote is to affirm it.

STATE OF NORTH CAROLINA, EX REL. UTILITIES COMMISSION; RUFUS L. EDMISTEN, ATTORNEY GENERAL; PUBLIC STAFF; HENRY J. TRUETT; TOWN OF BRYSON CITY; SWAIN COUNTY BOARD OF COUNTY COMMISSIONERS; CHEROKEE, GRAHAM AND JACKSON COUNTIES, THE TOWNS OF ANDREWS, DILLSBORO, ROBBINSVILLE, AND SYLVA; THE TRIBAL COUNCIL OF THE EASTERN BAND OF CHEROKEE INDIANS; MURIEL MANEY; AND DEROL CRISP v. NANTAHALA POWER AND LIGHT COMPANY; ALUMINUM COMPANY OF AMERICA; AND TAPOCO, INC.

No. 8210UC1034

(Filed 6 December 1983)

1. Electricity § 3; Utilities Commission § 36— electric rates—affiliated utilities—use of energy generated by unified system rather than entitlements under agreements

Where the Utilities Commission found that Nantahala Power Co. and Tapoco, Inc. should be treated as one utility for ratemaking purposes, and where Nantahala, Tapoco, TVA and Alcoa had entered into agreements approved by the Federal Energy Regulatory Commission under which all power generated by Nantahala and Tapoco is to be delivered to TVA, certain annual demand and energy entitlements are granted to Nantahala and Tapoco, and Alcoa, Nantahala and Tapoco are to decide how the power will be divided between Nantahala and Tapoco, the Utilities Commission's use of the amount of energy generated by the unified system in setting Nantahala's rates to its retail customers rather than the energy received as entitlements under the agreements with TVA, Alcoa and Tapoco did not constitute a modification of such agreements and was proper.

2. Electricity § 3; Utilities Commission § 36— electric rates—affiliated utilities—costs of energy—no violation of Commerce Clause

The Utilities Commission's method of determining the retail rates of Nantahala Power Co. on the basis of its percentage of the costs of the energy generated and purchased by the combined Nantahala-Tapoco system did not shift a portion of Nantahala's costs to its Tennessee customers in violation of the Commerce Clause of the U.S. Constitution. Art. I, § 8 of the U.S. Constitution.

3. Electricity § 3; Utilities Commission § 57— independent finding by Utilities Commission—sufficiency of evidence

The Utilities Commission made an independent finding of fact not based on a prior Supreme Court decision in the case that energy demand and entitlement agreements entered into by Nantahala Power Co., Tapoco, Inc., TVA and Alcoa resulted in substantial benefits to Alcoa to the detriment of Nantahala's customers, and such finding was supported by the evidence at a rate hearing although there was contrary evidence tending to show that the agreements were fair to Nantahala.

4. Electricity § 3; Utilities Commission § 36— electric rates—affiliated companies—method of roll-in of properties, revenues and expenses

The Utilities Commission was not required by a Supreme Court opinion remanding this case to adopt a method of rolling in the properties, revenues and expenses of Tapoco, Inc. with those of Nantahala Power Co. which acknowledged apportionment agreements entered by Nantahala, Tapoco, TVA and Alcoa as controlling the allocation of costs and benefits in determining Nantahala's retail rates. Nor was the Commission required to make a distinction between firm power and curtailable power.

5. Electricity § 3; Utilities Commission § 36— electric rates—affiliated utilities—roll-in of properties, revenues and expenses—failure to include power purchased by parent company

The Utilities Commission's roll-in of the properties, revenues and expenses of Tapoco, Inc. with those of Nantahala Power Co. for the purpose of determining Nantahala's retail rates was not erroneous because it included the power which Nantahala purchased from TVA but did not include the power which its parent company, Alcoa, purchased from TVA.

6. Utilities Commission § 5— parent corporation as public utility—constitutionality of statute

The statute providing for the imposition of public utility status on certain parent corporations, G.S. 62-3(23), is not void for vagueness, since a person of ordinary understanding would know from reading the statute that if a parent corporation controls its wholly owned public utility in such a way that the rates of the utility are affected, this has an effect on the rates and the parent corporation could be found to be a public utility.

7. Utilities Commission § 5— parent corporation as public utility—no delegation of legislative power

The statute providing for the imposition of public utility status on certain parent corporations, G.S. 62-3(23), does not delegate legislative power to the Utilities Commission in violation of Art. I, § 6 of the N.C. Constitution, since the legislature has given the Utilities Commission sufficient guidelines so that if the facts are properly found by the Commission, it does not make policy but carries out legislative policy.

8. Electricity § 3; Utilities Commission § 36— extent of affiliation on rates—sufficiency of finding

A finding by the Utilities Commission that "Alcoa has so dominated certain transactions and agreements affecting its wholly owned subsidiary Nantahala that Nantahala has been left but an empty shell, unable to act in its own self interest, let alone the interest of its public utility customers in North Carolina" was a sufficient finding as to the extent Alcoa's affiliation with Nantahala had affected the rates of Nantahala within the purview of G.S. 62-3(23)c

so as to support the Commission's order that Alcoa must pay any portion of refunds to Nantahala's customers which Nantahala is financially unable to pay.

9. Electricity § 3; Utilities Commission § 36— electric rates—responsibility of parent corporation for refunds—no retroactive ratemaking

A Utilities Commission order requiring Alcoa to be responsible for a refund to customers of Nantahala Power Co. for a period of time prior to the time Alcoa was held to be a public utility did not constitute retroactive ratemaking.

10. Electricity § 1; Utilities Commission § 5— Tapoco, Inc. as public utility

The Utilities Commission properly found that Tapoco, Inc. is a public utility where the evidence showed that electricity generated by Tapoco is exchanged with TVA for power from TVA, since this constitutes furnishing electricity to TVA for distribution to the public within the meaning of G.S. 62-3(23)b.

11. Electricity § 3; Utilities Commission § 36— electric rates—affiliated utilities—single electric system

The Utilities Commission properly found that Nantahala Power Co. and Tapoco, Inc. constitute a single integrated electric system operated as a coordinated part of the TVA system where the evidence showed that the two companies traded all their generation to TVA and received from TVA entitlements to energy which they divide as they please.

12. Electricity § 3; Utilities Commission § 47— general rate case—notice to parent of possible responsibility for subsidiary's refunds

When Alcoa was held to be a public utility and was made a party to a general rate case, it received adequate notice that it might be held liable for a refund to retail customers of its wholly owned subsidiary, Nantahala Power Co.

13. Utilities Commission § 44— general rate case—prefiling of testimony—time for filing brief

The due process rights of Alcoa in a general rate case involving its wholly owned subsidiary, Nantahala Power Co., were not violated by the Utilities Commission's requirement that Alcoa prefile its testimony prior to the prefiling of the intervenors' testimony and that Alcoa file its brief concurrently with that of the intervenors.

14. Utilities Commission § 36— electric rates—finding concerning affiliated companies—no shifting of burden of proof

Although the Utilities Commission stated in its rate order that it had permitted Alcoa to introduce evidence "to challenge the findings of the Supreme Court" in a prior appeal of the case that Nantahala Power Co. and Tapoco, Inc. constituted a single electric system for ratemaking purposes, the Commission did not improperly shift the burden of proof to Alcoa where there was sufficient evidence to support the Commission's finding that Nantahala and Tapoco constituted a single system for ratemaking purposes without the use of any presumption against Alcoa.

15. Electricity § 3; Utilities Commission § 36— electric rates—responsibility of parent for subsidiary's refunds—general rate case

A proceeding in which the Utilities Commission found Alcoa to be a public utility and ordered Alcoa to pay any portions of refunds which its wholly owned subsidiary, Nantahala Power Co., is financially unable to pay was properly conducted as a general rate case rather than as a complaint proceeding against Alcoa, since the responsibility of Alcoa for Nantahala's refund was ancillary to the case.

16. Electricity § 3; Utilities Commission § 56— electric rates—order for refunds—compliance with prior Supreme Court decision

The Utilities Commission was following the mandate of the N.C. Supreme Court in a prior appeal of this case in ordering Nantahala Power Co. to "refund to its North Carolina retail customers all revenue collected under the rates approved by the Commission order issued June 14, 1977, to the extent that said rates produce revenue in excess of the rates approved herein."

17. Electricity § 3; Utilities Commission § 36— electric rates—order requiring refunds—no confiscation of property

A Utilities Commission order providing for refunds to Nantahala Power Company's retail customers and requiring Nantahala's parent company, Alcoa, to pay any portion of the refunds which Nantahala is financially unable to pay did not confiscate the property of Nantahala in violation of its due process rights because Nantahala's refund obligation is more than its net worth, Alcoa has denied its obligation to pay, and it may be years before Alcoa has exhausted its remedies in federal court.

APPEAL by respondents from order of North Carolina Utilities Commission entered 2 September 1981. Heard in the Court of Appeals 25 August 1983.

This is an appeal from an order by the North Carolina Utilities Commission reducing rates and requiring a refund by Nantahala Power and Light Company and Alcoa. This case has previously been in the appellate courts. *See Utilities Comm. v. Edmisten, Attorney General*, 40 N.C. App. 109, 252 S.E. 2d 516 (1979), *aff'd in part and rev'd in part*, 299 N.C. 432, 263 S.E. 2d 583 (1980). Nantahala and Tapoco, Inc. are wholly owned subsidiaries of the Aluminum Company of America (Alcoa). Each of them is engaged in the generation of hydroelectric power in western North Carolina. Tapoco sells power to no one but Alcoa for the use of its aluminum manufacturing operations in Tennessee. Nantahala, which was organized in 1929, served the public until 1941 with a small amount of its power going to Alcoa. In 1941 with the advent of World War II, Nantahala accelerated the development

of its hydroelectric power to serve Alcoa's increased production of aluminum for the war effort. After the war, Alcoa continued buying power from Nantahala but the expanded demand by the public took increasing amounts of Nantahala's generation so that after 1971 Alcoa has not taken any power from Nantahala.

In 1941 Nantahala and Tapoco entered into an agreement with the Tennessee Valley Authority (TVA) known as the Fontana Agreement. Among other things, this agreement provided that the TVA would coordinate the water flow of the dams owned by Nantahala and Tapoco. The agreement was to last for 20 years. In 1962 the Fontana Agreement was replaced by the New Fontana Agreement (NFA). TVA, Alcoa, Nantahala and Tapoco are parties to the NFA. Under the terms of the NFA, all power generated by Nantahala and Tapoco is delivered to TVA. TVA grants to Nantahala and Tapoco annual entitlements to some 1,798,000,000 kwh. The NFA provides that Alcoa, Nantahala and Tapoco will decide how the power will be divided between Nantahala and Tapoco.

In 1963 an agreement was made by the three parties under the terms of which Nantahala was to receive as its monthly share of the NFA entitlements the larger of either its total actual generation or 30,000,000 kwh. This agreement provided further that Alcoa was to pay Nantahala an annual sum of $89,200 in compensation for allowing TVA to control the flow of water through Nantahala's dams.

In 1971 a new apportionment agreement was made. Under this agreement Nantahala received 360 million kwh annually. The $89,200 annual payment from Alcoa was eliminated and Nantahala purchased from TVA any additional power it needed for its customers. In 1975, the test year for this case, Nantahala purchased slightly more than 90 million kwh from TVA for which it paid over $1.5 million dollars. Nantahala generated in excess of 520 million kwh in that year.

The Utilities Commission first refused to join Alcoa and Tapoco as parties and denied a motion to compel Nantahala to produce information sufficient to allow the Commission to consider a rate design based on the "rolling in" of Tapoco's properties, revenues and expenses with those of Nantahala, as though the two were operating as one utility. This Court reversed. Our

Supreme Court affirmed in part the decision of this Court and ordered the case remanded to the Utilities Commission with directions that it consider whether a rate schedule computed as if Nantahala and Tapoco were one utility would be in the best interests of the customers of Nantahala.

After the remand from the Supreme Court, the Utilities Commission held further hearings. Alcoa and Tapoco were made parties to the proceedings and were held to be public utilities. The Commission found that the NFA and the 1971 Apportionment Agreement have resulted in substantial benefits to Alcoa to the significant detriment of the retail customers of Nantahala, and that the Nantahala and Tapoco systems should be treated as one entity with respect to all matters affecting the determination of Nantahala's reasonable cost of service applicable to its North Carolina retail operations.

In calculating the costs of power to Nantahala's retail customers, the Utilities Commission did not use the NFA or 1971 Apportionment Agreement. It used instead the total generation of Nantahala and Tapoco plus the power purchased from TVA by Nantahala. It allocated Nantahala's share of demand related costs by dividing the total dependable capacity of the two systems plus the power purchased from TVA into Nantahala's peak load during the test year. The result was 24.60% which the Commission assigned to Nantahala as its percent of the total system demand costs. It calculated Nantahala's share of energy related costs by dividing total average energy available from the unified system plus Nantahala's purchase from TVA into Nantahala's energy requirements for 1975. This gave a result of 24.51% which the Commission assigned to Nantahala as its share of energy costs for the unified system.

The Commission ordered that Nantahala reduce its rates and refund to its North Carolina retail customers all revenue collected under the Commission's order issued 14 June 1977 to the extent said rates produced revenue in excess of the rates allowed by the Commission in this proceeding. It ordered further that to the extent Nantahala is financially unable to make the refunds required in the Commission's order, Alcoa shall make such refunds.

Alcoa, Nantahala and Tapoco appealed.

Attorney General Edmisten, by Assistant Attorney General Richard L. Griffin, for the State.

Crisp, Davis, Schwentker and Page, by William T. Crisp and Robert B. Schwentker, for Henry J. Truett, the Counties of Cherokee, Graham, Swain, and Jackson; the Towns of Andrews, Dillsboro, Robbinsville, Bryson City and Sylva; and the Tribal Council of the Eastern Band of the Cherokee Indians.

Robert Fischbach, Executive Director of The Public Staff, by Staff Attorney Thomas K. Austin, for the Using and Consuming Public.

Joseph A. Pachnowski for the Town of Bryson City.

Western North Carolina Legal Services, Indian Law Unit, by Larry Nestler, for Muriel Maney and Derol Crisp.

Fred H. Moody, Jr. for the County of Swain.

Hunton and Williams, by Robert C. Howison, Jr., James E. Tucker, Edward S. Finley, Jr., and William C. Matthews, Jr., for Nantahala Power and Light Company.

LeBoeuf, Lamb, Leiby and MacRae, by Ronald D. Jones and David R. Poe, for Aluminum Company of America and Tapoco, Inc.

WEBB, Judge.

[1] Nantahala and Tapoco first attack the methodology used by the Utilities Commission in establishing the charge to Nantahala's retail customers. They argue that the Commission is required by law to recognize the NFA and the 1971 Apportionment Agreement in setting rates for Nantahala's retail customers. They say this is so because both of these agreements have been filed with and approved by the Federal Energy Regulatory Commission (FERC) and the Utilities Commission is preempted by federal law from ignoring them. The Utilities Commission in setting retail rates has to give effect to wholesale rates established by the FERC. *See F.P.C. v. Southern California Edison Co.*, 376 U.S. 205, 84 S.Ct. 644, 11 L.Ed. 2d 638, *reh'g denied, F.P.C. v. Southern California Edison Co.*, 377 U.S. 913, 84 S.Ct. 1161, 12 L.Ed. 2d 183 (1964); *Public Service Co. of Colorado v. P.U.C. of Colorado*, 644 P. 2d 933 (Colo. 1982); *People's Counsel of D.C. v. P.S.C. of D.C.*, 444 A. 2d 975 (D.C. Ct. App. 1982); *Northern States Power Co. v. Hagen*, 314 N.W. 2d 32 (N.D. 1981); *Narragansett Electric Co. v. Burke*, 119 R.I. 559, 381 A. 2d 1358 (1977), *cert. denied, Burke v. Narragansett Electric Co.*, 435 U.S. 972, 98 S.Ct. 1614, 56 L.Ed. 2d 63 (1978); *Citizens Gas Users Ass'n. v. Public Utilities Comm.*, 165 Ohio St. 536, 138 N.E. 2d 383 (1956); *City of Chicago v. Illinois Commerce Comm.*, 13 Ill. 2d 607, 150 N.E. 2d 776 (1958); and *United Gas Corp. v. Mississippi P.S.C.*, 240 Miss. 405, 127 So. 2d 404 (1961). Nantahala and Tapoco contend that when the Utilities Commission, in setting retail rates for Nantahala, refused to use the demand and energy entitlements which Nantahala received under the NFA and the 1971 Apportionment Agreement, the Commission modified these two agreements which it does not have the power to do.

We believe the resolution of this case largely depends on a proper analysis of the NFA and the 1971 Apportionment Agreement as affected by the order of the Utilities Commission. The Commission's order does not change the energy entitlements received by Nantahala and Tapoco under the NFA and the 1971 Apportionment Agreement. Each receives its share of the power and uses it as received. The question is whether by not using these two agreements in setting Nantahala's rates the Utilities Commission has changed the agreements, which it does not have the power to do.

When the Utilities Commission determined that Nantahala and Tapoco should be treated as one company for rate-making purposes, it was faced with the question of what constituted a proper charge to Nantahala's retail customers for the power used by them. The Utilities Commission resolved this question by assigning to Nantahala's retail customers a demand charge based on the percentage used by Nantahala of the firm energy generated and purchased by the unified system during the test year. It calculated the energy charge using the same method, that is, it assigned to Nantahala's customers the percentage needed for their own energy requirements out of the total energy generated and purchased by the unified system.

The amount of energy generated by the unified system was not the same as the energy Nantahala received as entitlements.

Therefore the question is whether the Commission has changed the NFA and the 1971 Apportionment Agreement by using generation rather than entitlements under the agreements in calculating retail rates for Nantahala. We believe by requiring Nantahala's retail customers to pay demand and energy charges based on Nantahala's percent of the demand and energy requirements from the capacity of the entire system the Utilities Commission has used a methodology we cannot disturb. The methodology calculates the cost of the generation which the unified system trades to TVA for the electricity used by the system. In whatever form the entitlement comes to Nantahala-Tapoco, Nantahala's customers should only be charged for Nantahala's share of the costs of what was traded for the entitlements. We do not believe the methodology used by the Utilities Commission changes the NFA or the 1971 Apportionment Agreement.

Nantahala and Alcoa also argue that Tapoco's four hydroelectric plants have been licensed by the FERC for the express purpose of supplying power to Alcoa's Tennessee operations and that by directing a part of Tapoco's power to Nantahala's customers, the order of the Utilities Commission has imposed a condition on a federal license to operate their plants which it may not do. *See First Iowa Hydro-Electric Cooperative v. F.P.C.*, 328 U.S. 152, 66 S.Ct. 906, 90 L.Ed. 1143, *reh'g denied*, 328 U.S. 879, 66 S.Ct. 1336, 90 L.Ed. 1647 (1946). We do not believe the Commission's order diverts power from Tapoco to Nantahala. The order fixes the costs to Nantahala for the power it receives through the NFA and the 1971 Apportionment Agreement.

[2] Nantahala and Alcoa contend that the order of the Commission places an impermissible burden on interstate commerce in violation of Article I, § 8 of the United States Constitution. The Commission recited in its order that "Nantahala-Tapoco combined system's North Carolina public load has first call on the total electric energy output of the combined system, and to the extent that said output exceeds the requirements of the North Carolina public load, such excess will be available for sale and will be purchased by Alcoa." Nantahala and Tapoco argue that it is a violation of the Commerce Clause to prefer the residents of one state over the residents of another state; and after stating it would do this, the Utilities Commission did so by the methodology it used

in setting Nantahala's retail rates. They argue that this methodology reduced Nantahala's rates below its costs and shifted these costs to the combined system's Tennessee load.

If the Utilities Commission had used a methodology that gave "first call" to the North Carolina customers it would violate the Commerce Clause. In spite of its recital, we do not believe the Utilities Commission did this. We believe that the methodology used by the Commission allows Nantahala to recover the costs of the percentage of energy it used based on its percentage of the costs of the energy generated and purchased by the combined system. We do not believe this prefers North Carolina customers over Tennessee customers.

Nantahala and Tapoco say that an illustration of the shifting of costs to out-of-state customers may be found in the way the demand cost allocation factor for Nantahala is calculated. Based on Nantahala's peak load which was 24.6% of the total firm capability of the combined system, the Commission assigned 24.6% of the demand costs to Nantahala. Nantahala and Tapoco point out that Tapoco's peak load was only 44.9% of the total firm capability of the combined system. They say that Tapoco is thus required to shoulder 75.4% of the demand costs, 30% more than its responsibility. We believe that in determining Nantahala's reasonable demand cost, the Commission was not required to assure the recovery of 100% of the demand costs incurred in the combined system. Nantahala's customers should not be required to pay more for demand than that for which they are responsible, even if it means that all the combined system demand costs are not recovered. *See Utilities Comm. v. Telephone Co.*, 281 N.C. 318, 189 S.E. 2d 705 (1972), *superseded by statute, Utilities Comm. v. Power Co.*, 305 N.C. 1, 287 S.E. 2d 786 (1982).

Nor do we believe *New England Power Co. v. New Hampshire*, 455 U.S. 331, 102 S.Ct. 1096, 71 L.Ed. 2d 188 (1982) governs this case. It was said in that case that "Our cases consistently have held that the Commerce Clause of the Constitution, Art. I, § 8, cl. 3, precludes a state from mandating that its residents be given a preferred right of access, over out-of-state consumers, to natural resources located within its borders or to the products derived therefrom." *Id.* at 338, 102 S.Ct. at 1100, 71 L.Ed. 2d at 197. The facts of that case are distinguishable from this case. In

that case the Supreme Court held that it was an impermissible burden on interstate commerce for the New Hampshire Public Utilities Commission to require a power company generating hydroelectric power in New Hampshire to sell an amount of power in New Hampshire at hydroelectric rates equal to the amount of hydroelectric power it generated in New Hampshire. In this case the Utilities Commission has set a rate for Nantahala-Tapoco based on the cost of producing the power.

Alcoa argues that it, Nantahala and Tapoco are regulated by TVA; that TVA has approved the NFA and the 1971 Apportionment Agreement, and the Utilities Commission cannot refuse to give effect to these agreements. As we have said, we do not believe the Utilities Commission has refused to give effect to these agreements. It has calculated the costs to Nantahala's customers of the power delivered to them under the agreements.

Alcoa also argues that the relationship between Alcoa, Nantahala and Tapoco is regulated by the Securities and Exchange Commission under the Public Utility Holding Company Act of 1935 and the SEC has granted the companies an exemption from some of the requirements of the Act. We do not believe the order of the Utilities Commission has in any way affected the order of the SEC as to the three companies.

[3] Nantahala assigns error to the Commission's finding of fact that the NFA and the 1971 Apportionment Agreement resulted in substantial benefits to Alcoa to the detriment of Nantahala's customers. Nantahala argues first that the Commission made no finding of fact that the two agreements were unfair to Nantahala's customers but erroneously assumed our Supreme Court had found as a fact that they are unfair. It argues further that the only evidence at the hearing after the Supreme Court's remand is that the agreements were fair. The Supreme Court questioned the fairness of an agreement which required Nantahala to purchase additional power regardless of the adequacy of its own generation. Nantahala's witness testified that the only valid way to compare generation is on an hour-by-hour basis, that a hydroelectric power plant can generate more power than its customers use during a year, but if the power cannot be generated when there is a demand for it, the power generated during the period when it is not needed is useless. Nantahala's

witness testified this was the case for Nantahala during the test year and for that reason, Nantahala benefited from the firm power it received under the NFA and 1971 Apportionment Agreement. Nantahala also contends that the Commission did not address the evidence that during the 12-month period from June 1980 through May 1981, Nantahala's generation was less than its entitlement under the NFA and the 1971 Apportionment Agreement. Finally, Nantahala contends no consideration was given to the substantial benefits Nantahala's customers have received since 1941 because of the presence of Alcoa. Nantahala argues that the uncontradicted evidence shows that the NFA and 1971 Apportionment Agreement are fair to Nantahala's customers and the Commission should have so found.

We believe the Utilities Commission made an independent finding of fact that the NFA and the 1971 Apportionment Agreement were unfair to Nantahala's customers. We believe a reading of our Supreme Court's opinion in the previous appeal in this case leaves little doubt that they considered the NFA and the 1971 Apportionment Agreement unfair to the customers of Nantahala. We cannot hold because of this, however, that the Commission's finding of fact on this issue, which we believe was supported by the evidence, was not independently made. The Commission did not comment on all the evidence as to the fairness of the two agreements but it was not required to do so.

The Commission relied on evidence that in 1963 an agreement had been made under which Nantahala received a minimum of 360,000,000 kwh annually plus its actual production in excess of 360,000,000 kwh. This allocation was based on engineering studies which showed that under the most adverse water conditions Nantahala could generate 360,000,000 kwh annually with the average energy that could be generated annually to be 439,000,000 kwh per year. Under the 1971 Apportionment Agreement, Nantahala received only 360,000,000 kwh per year. The additional power which Nantahala had received under the 1963 agreement went to Tapoco and was passed on to Alcoa. There was evidence that the peaking capacity allotted Nantahala under the 1971 Apportionment Agreement is less than its actual capacity. This results in Nantahala having to pay a demand charge to TVA when Nantahala's customers demand is less than Nantahala's capacity. Nantahala's dams are upstream from Tapoco's dams. This means

Nantahala can store water during the winter months and, by releasing it in dry seasons, can provide water for Tapoco. This benefit to Tapoco was not taken into account in the 1971 Apportionment Agreement.

The Commission also relied on evidence that under the 1941 Fontana Agreement, Nantahala gave TVA the right in perpetuity to control the storage and flow of water from its hydroelectric projects. This constituted a loss of considerable value to Nantahala which the TVA recognized in the return entitlements of the NFA. Nantahala was paid $89,200 per annum by Alcoa for this loss under the 1963 agreement but received nothing for it under the 1971 Apportionment Agreement. There is evidence in the record which shows it is some benefit to TVA for Nantahala to be integrated into the TVA system. TVA recognized this in the NFA but no benefits were given to Nantahala in the 1971 Apportionment Agreement for this right.

There was evidence that the NFA is unfavorable to Nantahala in that it is structured to meet Alcoa's needs and not the needs of Nantahala. This is so because the return entitlement is structured to meet Alcoa's demand for a certain amount of stable electricity for purposes of aluminum production. It is not structured to meet Nantahala's need for peaking capacity which a utility with a public service load requires. Nantahala has a need for assured, but constantly variable amounts. It has this peaking capacity but it does not receive it under the NFA. We believe this evidence supports the Commission's finding of fact that the NFA and the 1971 Apportionment Agreement resulted in substantial benefits to Alcoa to the significant detriment of Nantahala's customers. There was substantial evidence that the two agreements were fair but this evidence was by no means uncontradicted. We cannot disturb this finding by the Utilities Commission.

[4] Nantahala contends that the Utilities Commission did not adopt a roll-in methodology within the scope of the remand by our Supreme Court. They argue that the Supreme Court envisioned a roll-in methodology which acknowledges the terms of the NFA and the 1971 Apportionment Agreement. Nantahala argues that the Supreme Court intended that the two agreements should be considered as valid and should control on the allocation of costs

and benefits on all matters to which they applied. Nantahala also argues that the methodology erroneously fails to draw any distinction between the value of firm power on the one hand and curtailable power on the other. Nantahala argues that curtailable power is of almost no value to a utility serving a public load because the public will not accept services that may require even short periods of darkness or lack of heat. Under the 1971 Apportionment Agreement, Nantahala received virtually all the firm power entitlements and Tapoco virtually all of the curtailable entitlements. Tapoco then had to pay TVA in order for TVA not to curtail power to Tapoco. Nantahala argues this should have been taken into account when adopting a roll-in methodology.

We do not agree that the Utilities Commission was required by the opinion of the Supreme Court to use a roll-in methodology that acknowledges the NFA and 1971 Apportionment Agreements as controlling as to costs and benefits. The Supreme Court did not prescribe a formula for a roll-in. In discussing the NFA and the 1971 Apportionment Agreement which the Court felt required Nantahala to purchase extra power for its customers although it generated sufficient power for them, the Court said that to suggest such an arrangement fairly served the customers of Nantahala "assaults the common sense of this Court." In light of this language by the Supreme Court, we do not feel its opinion requires the roll-in to be based on the NFA and 1971 Apportionment Agreement. It is true that the Supreme Court did not consider the federal questions in its opinion. We believe the Utilities Commission stayed within the mandate of the Supreme Court and it violated no federal law in so doing. The Utilities Commission was not required to consider payments made by Tapoco to prevent the curtailment of power because this did not occur in the test year.

Alcoa also contends that the roll-in applied by the Utilities Commission is not in conformity with the opinion of the Supreme Court. Alcoa points out that the Supreme Court's concern was with the fact that Nantahala did not receive the fair economic equivalent of what its generating plants were capable of producing as a result of which Nantahala was forced to purchase expensive TVA power. Alcoa argues that an analysis of the NFA and the 1971 Apportionment Agreement shows that Tapoco and Alcoa did not receive any hidden benefits from them. The unified

system did not receive as much in the entitlements as the system generated and Alcoa says this is because Nantahala's harvests of energy are neither as regular nor abundant as the Supreme Court was led to believe. This is because there is a substantial mismatch in the times at which the power is generated and the times it is needed. For this reason, TVA was not willing to give an entitlement of firm power equal to the generation of the unified system. Alcoa argues that the analysis which the Commission should have made and failed to do was whether the division of the entitlements between Nantahala and Tapoco was equitable. It says that any study of the division of these entitlements shows that Tapoco faired far worse than Nantahala in that it received less power in return for its contribution than did Nantahala. The Commission did analyze the 1971 Apportionment Agreement as well as the NFA as pointed out in another part of this opinion. It came to the conclusion that they were unfair to Nantahala's customers. We might reach a different conclusion but it is not for us to dictate to the Utilities Commission the weight to give material facts before it. We believe the weight the Commission gave to these facts was within the requirements of the Supreme Court's opinion.

[5] Alcoa also objects to the roll-in because it includes the power which Nantahala purchased from TVA but does not include the power which Alcoa purchased from TVA. We believe the Commission was correct in not considering the power purchased by Alcoa from TVA. The Commission's task was to determine the part Nantahala's retail customers should be required to pay for their share of the energy received by the unified Nantahala-Tapoco system under the NFA and purchased from TVA. They should not be required to pay for energy purchased by Alcoa outside the unified system.

Alcoa assigns error to the Commission's finding that Alcoa is a public utility and its requirement that Alcoa pay any portion of the refunds which Nantahala is financially unable to make. The Utilities Commission found Alcoa to be a public utility pursuant to G.S. 62-3(23)c which provides:

> The term "public utility" shall include all persons affiliated through stock ownership with a public utility doing business in this State as parent corporation or subsidiary corporation as defined in G.S. 55-2 to such an extent that the Commission shall find that such affiliation has an effect on the rates or service of such public utility.

Alcoa attacks this portion of the Utilities Commission's order on three grounds. It says (1) G.S. 62-3(23)c is unconstitutional for vagueness, (2) it constitutes an unlawful delegation of legislative authority, and (3) the Commission misinterpreted and misapplied this section of the statute.

[6] Under the due process clause of the Fourteenth Amendment to the United States Constitution, a statute is void for vagueness if its terms are so vague, indefinite and uncertain that a person cannot determine its meaning and therefore cannot determine how to order his behavior so as to avoid its dictates or avoid its application. *See Lanzetta v. New Jersey*, 306 U.S. 451, 59 S.Ct. 618, 83 L.Ed. 888 (1939) and *State v. Poe*, 40 N.C. App. 385, 252 S.E. 2d 843, *cert. denied*, 298 N.C. 303, 259 S.E. 2d 304 (1979), *appeal dismissed*, 445 U.S. 947, 100 S.Ct. 1593, 63 L.Ed. 2d 782 (1980). Alcoa argues that the legislature has failed to define what the effect on rates or services is necessary to impose public utility status on a parent corporation, and there is thus no guidance for the Commission as to whether Alcoa has had an effect on Nantahala. It argues further that a reading of the statute gives no indication of the parent company actions that the legislature was attempting to control or eliminate. We believe a person of ordinary understanding would know from reading the statute that if a parent corporation controls its wholly owned public utility in such a way that the rates of the utility are affected this has an effect on the rates and the parent corporation could be found to be a public utility. This prevents this section of the statute from being void for vagueness.

[7] Alcoa contends that G.S. 62-3(23)c violates Article I, § 6 of the North Carolina Constitution because it delegates legislative power to the Utilities Commission. It says this is so because it is a legislative decision as to what shall be a public utility and that by enacting this section of the statute, the legislature has allowed the Commission to determine what corporations shall be designated public utilities and how they shall be regulated without adequate legislative standards to guide the Commission. We believe, without discussing all the hypothetical situations that on

the facts of this case there has not been a delegation of legislative authority. In order to find that Alcoa is a public utility, the statute required the Utilities Commission to find that Alcoa was so affiliated with Nantahala as to have an effect on Nantahala's rates. The Commission so found and we believe this finding was supported by the evidence. We believe that the General Assembly has given the Utilities Commission sufficient guidelines so that if the facts are properly found by the Commission, it does not make policy but carries out legislative policy. By the same token when the Utilities Commission determined that Alcoa is a public utility we believe it was legislative policy and not the Commission's policy under which the Commission required Alcoa to be responsible for a part of the refund.

[8] Alcoa also contends the Utilities Commission has misinterpreted and misapplied G.S. 62-3(23)c. It argues that since the section contains the words "to such an extent," the Commission may only regulate to the extent of the precise impact Alcoa has had on the rates of Nantahala. It argues that the Utilities Commission did not attempt to determine the extent to which Alcoa's relationship with Nantahala has affected Nantahala's rates and services and thus did not comply with the mandate of G.S. 62-3(23)c. Assuming that Alcoa is correct in this argument the Commission found the following: "Alcoa has so dominated certain transactions and agreements affecting its wholly owned subsidiary Nantahala that Nantahala has been left but an empty shell, unable to act in its own self interest, let alone the interest of its public utility customers in North Carolina." We believe this finding by the Commission is sufficient as to the extent Alcoa's affiliation with Nantahala had affected the rates of Nantahala so as to support the order of the Commission.

[9] Alcoa also contends the Commission has engaged in retroactive ratemaking which it does not have the power to do. *See Utilities Commission v. City of Durham*, 282 N.C. 308, 193 S.E. 2d 95 (1972). It says this is so because the rates established in this proceeding are for the period from July 1977 through August 1981 and Alcoa was not held to be a public utility until October 1980. Alcoa argues that to make it responsible for a refund prior to the time it was declared a public utility is retroactive ratemaking. Retroactive ratemaking occurs when a rate is set so as to permit collection in the future for expenses attributable to past

services. Alcoa was made responsible for a refund ordered for Nantahala for the period in question in this proceeding. We do not believe that it is retroactive ratemaking for Alcoa to be held responsible for a refund. The fact that it was not made a party to the proceeding until after the remand from the Supreme Court makes no difference.

[10] Tapoco assigns error to the Utilities Commission's finding that it is a public utility. The Commission found that Tapoco was a public utility under G.S. 62-3(23)a which provides a "person" is a public utility if it generates electricity for sale to the public. It also found Tapoco to be a public utility under G.S. 62-3(23)b which provides:

> The term "public utility" shall for rate-making purposes include any person producing, generating or furnishing any of the foregoing services to another person for distribution to or for the public for compensation.

The Commission advanced as a third reason for finding Tapoco to be a public utility that it had obtained from the Utilities Commission in 1955 a certificate of public convenience and necessity. The Commission found as a fourth reason for holding Tapoco is a public utility was that its articles of incorporation state that one of its purposes is to produce and provide electric power to the public and provide it with the powers of eminent domain.

We do not decide whether the Commission was correct in holding Tapoco to be a public utility as provided by G.S. 62-3(23)a because it holds a certificate of public convenience and necessity or because its articles of incorporation state that one of its purposes is to generate electricity for sale to the public. We do not believe that determination is necessary for a decision in this case. We believe the evidence is sufficient to find Tapoco is a utility for ratemaking purposes. Tapoco's generation is exchanged with TVA for power from TVA. We believe this constitutes furnishing electricity to TVA for distribution to the public for compensation. This would make Tapoco a public utility for ratemaking purposes. Although the Utilities Commission did not set a rate for Tapoco, the price Tapoco charges for electricity will be affected by the outcome of this case. We hold that for this case Tapoco is a utility for ratemaking purposes and is a proper party to the case.

Tapoco also contends that the decision of the FERC in *Town of Highlands v. Nantahala Power and Light Company*, 19 F.E.R.C. (CCH) ¶ 61 (14 May 1982), holding that Nantahala and Tapoco should not be treated as one utility for ratemaking purposes, is binding on this Court. The FERC, while holding that it would not roll-in the costs of the two companies, held that the 1971 Apportionment Agreement was unfair in that Nantahala does not receive under it the energy in proportion to its contribution under the NFA. We do not believe the action of the Utilities Commission in this case is inconsistent with the decision of the FERC. The FERC was passing on wholesale rates and did not attempt to set retail rates in North Carolina.

[11] Tapoco argues that the Commission's finding that Nantahala and Tapoco constitute a single integrated electric system operated as such by and as a coordinated part of the TVA system is arbitrary and capricious and not based on substantial evidence. It argues that the evidence shows that the two companies operate independently of each other, that they serve different customers and are regulated by different agencies. Finally, Tapoco argues that the historical development of the two companies is such that they cannot be considered one integrated system. These facts may have been sufficient for the Commission to have found that the two companies were not a single, integrated electric system but there were other facts. The two companies traded all their generation to TVA and received in exchange for this entitlements of energy which they divide as they please. We believe the Commission could conclude from these facts that the two companies constitute a single, integrated system for ratemaking purposes.

Tapoco also argues the Commission did not properly consider the evidence because it gave too much weight to what it called the findings of the Supreme Court. Tapoco points out that the Supreme Court cannot make findings of fact and for the Utilities Commission to refer to findings by the Court, which "findings" were made before Tapoco was a party to the proceedings is error. Tapoco argues that no weight should be given to this language of the Supreme Court. Although the Utilities Commission referred to some of the statements in the Supreme Court's opinion as findings we believe the Commission made its own findings based on competent evidence which we cannot disturb.

Finally, Tapoco argues that it was denied due process of law in the manner in which the hearing was conducted. It contends that it was entitled to notice as to the effect of holding it to be a public utility. It says that to hold it to be a public utility without defining what its duties would be in the future, thus leaving it with a Damoclean sword over its head, deprives it of due process. We have affirmed the holding of the Utilities Commission to the extent that Tapoco is held to be a public utility for purposes of this case and bound by any order entered in this case. We do not believe this leaves a Damoclean sword over the head of Tapoco.

[12] Alcoa argues that it was denied due process for several reasons. It says first that it was not given adequate notice of what it would be required to defend. It contends it was not put on notice that it might be required to be responsible for a part of the refund until the issuance of the Commission's order on 2 September 1981. Alcoa argues that the failure to be notified of what the issues would be deprived it of due process of law. *See Morgan v. United States*, 304 U.S. 1, 58 S.Ct. 773, 82 L.Ed. 1129 (1938). In this case Alcoa was made a party to the proceedings and held to be a public utility by order of the Commission on 3 October 1980. We believe that when Alcoa was held to be a public utility and made a party to a general rate case this was adequate notice that it might be held liable for the refund.

[13] Alcoa also contends its due process rights were violated by requiring it to prefile its testimony prior to the prefiling of the intervenors' testimony and requiring it to file its brief concurrently with the intervenors. It argues that it had a right to know what the contentions of the intervenors would be with a chance to meet them which it did not have under the procedure used by the Utilities Commission. Alcoa argues that it did not know the position of the intervenors as to the hidden benefits to Alcoa under the NFA and the 1971 Apportionment Agreement until the intervenors' brief was filed with the Utilities Commission at which time it did not have a chance to meet these contentions. We believe that in a general rate case to which Alcoa was a party and in which the NFA and the 1971 Apportionment Agreement were integral parts of the case Alcoa should have been forewarned that the intervenors intended to show the agreements were beneficial to Alcoa at the expense of Nantahala's customers. We hold the

procedure by which the Commission required Alcoa to prefile its testimony and its brief did not violate its due process rights.

Alcoa next contends it was deprived of due process by the Commission's consideration of evidence introduced at the hearings before it was made a party. There was sufficient evidence introduced at the hearings to which Alcoa was a party to support the Commission's findings of fact. We assume the Commission relied on this evidence.

[14] Alcoa next contends that the Utilities Commission improperly shifted the burden of proof. In its order the Utilities Commission made the following statement:

> These findings by the Supreme Court, that Nantahala and Tapoco constitute a single, integrated electric system and should be treated as one system for rate-making purpose [sic], have been carefully considered by the Commission for purposes of this proceeding. However, since Alcoa and Tapoco were not parties to the original proceeding that led to the June 14, 1977 Order, the Commission has allowed them and Nantahala to introduce evidence in the remand proceeding to challenge the findings of the Supreme Court.

Alcoa argues that by treating statements in the Supreme Court's opinion as findings of fact and requiring it to challenge them, the Commission placed a burden of proof on Alcoa which constitutes error. We do not believe we can hold the Utilities Commission placed the burden of proof on Alcoa. It did not say that it did so and there is sufficient evidence for the Commission to find the facts as it did without the use of any presumption against Alcoa. It is unfortunate that the Utilities Commission used the language it did since the Supreme Court did not and could not find facts. Nevertheless, we do not believe this language requires us to reverse the Utilities Commission.

[15] Alcoa's last argument is that the Commission violated its own rules by conducting the hearing as a general rate case and not as a complaint proceeding against Alcoa without the procedural rules of a complaint proceeding which could have given a different result. We believe the Utilities Commission was correct in conducting the proceeding as a general rate case. The primary question was what is a fair rate of return on Nantahala's invest-

ment so as to enable it by sound management to pay a fair profit to its stockholders and to maintain and expand its facilities and services in accordance with the reasonable requirement of its creditors. This would make it a general rate case. *See Utilities Comm. v. Gas Co.*, 259 N.C. 558, 131 S.E. 2d 303 (1963). The responsibility of Alcoa for Nantahala's refund was ancillary to the case.

[16] Nantahala assigns error to the Commission's requirement that it "refund to its North Carolina retail customers all revenue collected under the rates approved by Commission order issued June 14, 1977, to the extent that said rates produce revenue in excess of the rates approved herein." It argues that neither G.S. 62-132 nor G.S. 62-135 authorizes the Utilities Commission to order this refund. The opinion of our Supreme Court contains the following language:

> "We believe that essential fairness to all the parties is best served by allowing the increased rates to remain in effect, conditional upon Nantahala's guarantee that it will in the future refund to its customers any overcharges should the new rates ultimately be deemed excessive. Accordingly, we . . . direct the Commission to obtain adequate assurances of Nantahala's willingness and continued ability to refund such overcharges as may ultimately result from imposition of the 1977 rate schedule." *Utilities Comm. v. Edmisten, Attorney General*, at 444, 263 S.E. 2d at 592.

We believe the Utilities Commission was following the mandate of the Supreme Court in this portion of the order. We would have to overrule the Supreme Court to sustain this assignment of error, which we cannot do.

[17] Finally, Nantahala argues that the order of the Commission confiscates the property of Nantahala and thus violates its due process rights. It contends that its refund obligation is more than its net worth and although Alcoa was ordered to pay so much of the refund obligation as Nantahala cannot pay and remain solvent. Alcoa denies its obligation to pay. Nantahala says it may be years before Alcoa has exhausted its remedies in federal court and in the meantime Nantahala will not be able to serve its customers if it is responsible for the refund. It argues that such an order cannot be in the best interests of its customers.

We have affirmed the order as being within the mandate of our Supreme Court's opinion. We do not believe Nantahala's due process rights have been violated. The Utilities Commission has ordered that Alcoa be responsible for a part of the refund. We do not believe we should hold that Alcoa will not pay it and Nantahala will have to pay the entire refund, leaving it bankrupt.

We believe the Utilities Commission has conducted hearings and entered an order within the mandate of the Supreme Court's opinion. The appellants make persuasive arguments, particularly as to the equities involved. Indeed a good argument could be made that the best friend Nantahala's customers have is Alcoa. It financed the building of large hydroelectric facilities at a time when Nantahala could not have justified constructing them for its public customers. Nantahala's customers have had for many years the benefit of these facilities built at 1941 costs. Nevertheless, these are not factors which the law allows to be taken into account in setting utility rates.

Affirmed.

Judges ARNOLD and BRASWELL concur.

APPENDIX C

Opinion Of The North Carolina Utilities Commission, dated September 2, 1981

State of North Carolina
Utilities Commission
Raleigh

DOCKET NO. E-13, SUB 29 [Remanded]

BEFORE THE
NORTH CAROLINA UTILITIES COMMISSION

In the Matter of

Application of Nantahala Power and Light Company for Authority to Adjust and Increase Its Electric Rates and Charges	ORDER REDUCING RATES AND REQUIRING REFUND

BY THE PANEL: This proceeding is before the Commission upon remand from the Supreme Court of North Carolina. *Utilities Commission* v. *Edmisten, Attorney General,* 299 N.C. 432 (1980).

In an Order of the Commission issued March 11, 1981, this proceeding was assigned to be heard by the panel.

This matter was originally commenced by the application of Nantahala Power and Light Company (hereinafter Nantahala, Applicant, or Company), filed November 3, 1976, for an increase in retail rates and for a revised Purchased Power Adjustment Clause. The Commission, on June 14, 1977, issued its Order approving the requested retail rate increase based upon a cost of service study using the 1975 test year data and approving the Purchased Power Adjustment Clause (hereinafter PPA). From the entry of that Order the Intervenors appealed to the North Carolina Court of Appeals, which vacated the Commission Order and remanded the matter to the Commission for further proceedings, including a direction by that Court that the Commission consider a "roll-in" of Tapoco, Inc., and Nantahala for the purpose of establishing Nantahala's retail rates. 40 N.C. App. 109 (1979). Nantahala appealed to the North Carolina Supreme Court.

On March 5, 1980, the Supreme Court handed down its decision in *Utilities Commission* v. *Edmisten, Attorney General,* 299 N.C. 432. In its opinion the Supreme Court affirmed the decision of the Court of Appeals, insofar as it directed this Commission to consider whether a rate schedule computed as if Nantahala Power and Light Company and Tapoco, Inc., were one utility (a "roll-in") would be in the best interests of the customers of Nantahala. The Court held as follows:

> "The Commission erred in giving only minimal consideration to the evidence suggesting the propriety of the roll-in device. The case is remanded with directions to the Commission to obtain and consider information and data showing what Nantahala's cost of service to its customers would be if this method of rate making were used and whether Nantahala's customers would benefit thereby." 299 N.C., at 443.

The Supreme Court left to the discretion of the Commission the choice of procedure to obtain the necessary information for this computation. The Supreme Court reversed that part of the Court of Appeals' decision which vacated the rate increase, holding at page 444:

> "The Commission's order of 14 June 1977 authorizing an increase in Nantahala's rates was vacated by the Court of Appeals. The effect of the Court of Appeals' decision was stayed, however, by this court's issuance of a writ of supersedeas pending the outcome of this appeal. Although that writ is hereby dissolved, we believe that essential fairness to all the parties is best served by allowing the increased rates to remain in effect, conditioned upon Nantahala's guarantee that it will in the future refund to its customers any overcharges should the new rates ultimately be determined excessive. Accordingly, we reverse the Court of Appeals' setting aside of the order of 14 June 1977 and direct the Commission to obtain adequate assurances of Nantahala's

willingness and continued ability to refund such overcharges as may ultimately result from imposition of the 1977 rate schedule."

The Supreme Court remanded the cause to the "Court of Appeals for remand to the Utilities Commission for further proceedings consistent with this opinion."

Upon remand to the Commission, the following events took place:

On May 9, 1980, the Intervenors in this docket (the Attorney General, Henry J. Truett, Town of Bryson City, and Swain County) filed with the Commission a Motion for Rehearing Before the full Commission. On May 19, 1980, Nantahala filed its Response to Motion for Rehearing before the full Commission.

On May 14, 1980, the Intervenors filed the following pleadings: Motion for Prehearing Conference; Motion for Hearing Respecting Applicant's Ability to Refund Possible Overcharges; Motion to Join Alcoa and Tapoco, Inc., as Parties.

In response to these Motions, Nantahala filed the following pleadings on June 4, 1980: Response to Motion for Prehearing Conference; Response to the Motion for Hearing Respecting Applicant's Ability to Refund Possible Overcharges; and Response to the Motion to Join Alcoa and Tapoco, Inc., as Parties.

On June 4, 1980, Aluminum Company of America (Alcoa) and Tapoco, Inc. (Tapoco), each filed a separate Response to Motion to Join Alcoa and Tapoco, Inc., as Parties. (On June 27, 1980, the Intervenors filed Intervenors' Reply to Applicant's Response to Motion for Rehearing Before the Full Commission and Intervenors' Reply to Applicant's Response to Motion for Refund of Possible Overcharges.)

On June 24, 1980, the Commission ordered that these motions and responses should be set for oral argument before the full

Commission on July 11, 1980. The matter came on for argument as scheduled. with Nantahala, Tapoco, Alcoa, and the Intervenors being present and represented by counsel.

On July 29, 1980, the Commission issued an Order Setting Hearing and Requiring Data and Testimony. This Order scheduled a hearing for August 28 (later rescheduled to August 29) to allow Tapoco and Alcoa to appear and contest the Commission's jurisdiction to join them as parties to this proceeding. This Order also provided that the increased rates approved in the Order of June 14, 1977, would remain in effect upon the filing of an Undertaking by Nantahala; that a hearing be scheduled beginning December 9, 1980, to consider information and data showing what Nantahala's cost of service to its customers would be if Nantahala and Tapoco were treated as a single system for rate-making purposes and to consider whether Nantahala's customers would benefit thereby; that Nantahala and Alcoa prefile certain information; and that Nantahala give Notice to the Public of the hearing.

The hearing de novo to determine whether Alcoa and Tapoco should be joined as parties to this proceeding was held on August 29, 1980.

On September 24, 1980, Motion was filed by Nantahala for an extension of time to answer data request and to prefile testimony and exhibits; an Order Granting Extensions of Time and Continuing Hearing of December 9, 1980, was issued on September 26, 1980.

On September 22, 1980, an Undertaking to Refund was filed by Nantahala.

Based upon the testimony and exhibits presented at the de novo hearing on August 29, 1980, the Commission issued an Order on October 3, 1980, declaring Alcoa to be a public utility in North

Carolina pursuant to G.S. 62-3(23)c. and subject to the jurisdiction of this Commission, and further declaring Tapoco to be a public utility in North Carolina and subject to the jurisdiction of this Commission, and ordering that each be made a party respondent in this proceeding.

On October 13, 1980, the Commission issued an Order Requiring Parties Alcoa and Tapoco to Comply with Data and Testimony Filings Rescheduling Hearing to March 31, 1981, and Requiring Public Notice.

On October 27, 1980, Joint Statement of Exceptions to the Commission Order of October 3, 1980, and Motion for Clarification was filed with the Commission by Alcoa and Tapoco. Response of Public Staff and Response of Intervenors to Alcoa and Tapoco's Motion for Clarification were filed on November 14, 1980.

On December 22, 1980, the Commission issued an Order Clarifying Procedures and Affirming Filing Schedules.

On January 16, 1980, Petition to Intervene was filed by Cherokee, Graham, and Jackson Counties, North Carolina; the Towns of Andrews, Dillsboro, Robbinsville, and Sylva, North Carolina; and the Tribal Council of the Eastern Band of Cherokee Indians. Nantahala filed response to this Petition on February 3, 1981.

On January 16, 1981, Motion to Expunge Data from the record was filed by all of the Intervenors in this matter, to which Responses by Nantahala and Tapoco and Alcoa were filed with the Commission on February 6, 1981. The data sought to be expunged related to the appreciation in value of the properties of all projects of Tapoco under license from the Federal Energy Regulatory Commission or its predecessor.

On February 5, 1981, all the Intervenors filed a Motion to Extend Filing of Prefiled Testimony and Exhibits to March 9, 1981, which was allowed by Commission Order of February 17, 1981.

On February 26, 1981, the Commission issued an Order Allowing Intervention of Cherokee, Graham, and Jackson Counties; the Towns of Andrews, Dillsboro, Robbinsville, and Sylva; and the Tribal Council of the Eastern Band of Cherokee Indians.

On March 11, 1981, the Commission issued an Order assigning the hearing to the panel, rather than the Commission, because of the heavy demands of the Commission's Calendar.

Motion to Intervene was filed with the Commission on March 13, 1981, by Muriel Maney, Route 1, Whittier, North Carolina, and allowed by appropriate Order.

On March 16, 1981, all of the Intervenors in this case filed Response to Respondents' Motion for Postponement of Date for Commencement of Hearings for Presentation and Cross-Examination of Witnesses.

Alcoa and Tapoco filed on March 18, 1981, their first set of data requests to the Public Staff and Intervenors.

On March 18, 1981, the Commission issued an Order Denying the Motion to Expunge Data.

On March 20, 1981, Motion to Reject for Filing Portions of Intervenors' Prefiled Testimony was filed by Respondents Alcoa and Tapoco.

On March 23, 1981, Respondents Alcoa and Tapoco filed answer to Intervenors' Motion to Strike the Testimony and Exhibits of Witnesses Little and Toof.

On March 23, 1981, there was filed with the Commission the Response of Alcoa and Tapoco to Intervenors' Motion to Require Alcoa and Tapoco to Join in the Execution of Nantahala's Undertaking to Refund or to Guarantee Nantahala's Continuing Financial Viability.

On March 24, 1981, the Commission issued an Order Denying the Motion of Alcoa and Tapoco for Postponement of Date for Commencement of Hearings and scheduled further hearings, if necessary, for May 18 through 20, 1981.

On March 27, 1981, Respondents' Second Set of Data Requests to the Public Staff and the Intervenors was filed with the Commission.

The proceeding came on for hearing as scheduled on March 31, 1981. Three public witnesses testified in support of the Intervenors: Marie Leatherwood; Veronica Nicholas, a County Commissioner of Jackson County; and Walter David McCoy, Chairman of the Tribal Council of the Eastern Band of Cherokee Indians. The Commission then heard oral argument on the motion previously filed by the Intervenors to Require Alcoa and Tapoco to Join in the Execution of Nantahala's Undertaking to Refund or to Guarantee Nantahala's Continuing Financial Viability. Upon conclusion of the arguments, the Commission deferred ruling on the Motion until a later date. On the afternoon of March 31 and continuing through April 1-3, April 7-9, and May 18-21, the Commission held hearings, the witnesses and the subject of their testimony being summarized as follows:

For Nantahala and the Respondents Alcoa and Tapoco: (1) John D. Russell of John D. Russell Associates, Inc., a public utility consulting firm, testified as to procedures he had used and the results obtained in preparing depreciation rates and depreciation accrual reserves for Tapoco; he also testified on the fair value of the Tapoco properties; (2) Robert D. Buchanan, the Assistant Controller—Financial Accounting of Alcoa, testified as to the 1975 year-end balance sheets of Nantahala and Tapoco, methods of making allowances for depreciation, Tapoco's capital structure, the combined operating income and expenses for Nantahala and Tapoco for the year ended December 31, 1975, rate of return for the two entities, and certain adjustments related to the forego-

ing data; (3) Herbert J. Vander Veen, a Principal in the Washington Utility Group of Ernst & Whinney, testified as to his proposed method for a rolled-in cost of service for Nantahala-Tapoco and as to his reasons why he did not think any type of roll-in was appropriate; (4) B.D. Cockrell, Alcoa's Operating Manager—Power, testified on the development of the Alcoa Tennessee operations, and of Tapoco and Nantahala and on why in his opinion the roll-in was not warranted; (5) David I. Toof, a supervisor in the Washington Utility Group of Ernst & Whinney, testified as to the Supreme Court's concern that Nantahala's relationship with Alcoa has had an adverse impact on Nantahala's ratepayers; as to certain of the analytical techniques used by Respondents' witness Little in an analysis of the impact that Alcoa has had on the rates paid by Nantahala's customers during the period 1940-1978; and as to how a "revenue requirement model was defined and developed, together with specific sets of assumptions which were used to produce alternative scenarios involving Nantahala's operations; (6) John M. Little, a manager in the Washington group of Ernst & Whinney, also testified as to the Supreme Court's concern that Nantahala's relationship with Alcoa has had an adverse impact on Nantahala's ratepayers; he also explained the results of studies conducted by him and Mr. Toof in which they analyzed the impact that Alcoa has had on Nantahala and its ratepayers, 1940-1978; (7) William M. Jontz, President and Chief Executive Officer of Nantahala, testified as to whether a rolled-in cost of service for Nantahala and Tapoco is appropriate for setting retail rates, and as to the history of the development of Nantahala; (8) George Popovich, Alcoa's power management consultant, testified on some of the factual circumstances surrounding the negotiations of the New Fontana Agreement during the period 1960-1962, and on the questions raised by the Supreme Court in its order remanding the instant case for further hearings; and (9) William J. Leininger, codirector of Ernst & Whinney's Washington, D.C., Group, testified as to "certain concerns" of the Supreme Court in remanding the instant case.

Prior to completion of Mr. Popovich's cross-examination, Assistant Attorney General Richard L. Griffin testified on his own behalf and on behalf of the Intervenor Attorney General as to certain communications between himself and a securities analyst concerning a securities arrangement that Nantahala had with First Union National Bank.

For the Intervenors: (1) Daniel A. Springs, head of the power supply planning and power system planning section of Southern Engineering Company of Georgia, testified as to his review and analysis of materials filed in this proceeding, including various contracts between or among Nantahala, Tapoco, Alcoa, and TVA; as to recommended appropriate capacity and energy allocation factors under a rolled-in allocation of cost responsibility of the Nantahala-Tapoco system; as to recommended separation of utility costs and revenues from nonutility costs and revenues. He also presented rebuttal to some of the testimony of the Nantahala, Alcoa, and Tapoco witnesses. (2) J. Bertram Solomon, electric rate consultant with Southern Engineering Company of Georgia, testified as to the revenues, expenses, and investments of Nantahala and Tapoco for the test year, as to whether a roll-in method of setting retail rates would benefit the retail customers, and as to an appropriate capital structure and rate of return for the Nantahala-Tapoco system.

In rebuttal to Intervenors' testimony, Nantahala and/or Alcoa and Tapoco sponsored testimony by the following witnesses: (1) N. Edward Tucker, Nantahala's Vice President for rates and regulation; (2) C.E. Pfeiffer, Alcoa's treasurer; (3) George Popovich; and (4) Herbert J. Vander Veen.

In addition to the testimony of the foregoing witnesses, virtually every one of them also sponsored one or more supporting exhibits.

Following the close of the hearings, the parties were requested to file briefs and proposed Findings of Fact and Conclusions of

Law on July 27, 1981 (later extended to August 5, 1981). The parties filed briefs and proposed orders in apt time.

Upon consideration of the testimony and exhibits presented at the hearing and the entire record in this docket, the Commission makes the following

FINDINGS OF FACT

1. Nantahala is a duly organized public utility company under the laws of North Carolina, subject to the jurisdiction of this Commission, and is holding a franchise to furnish electric power in the western part of the State of North Carolina under rates and service regulated by this Commission as provided in Chapter 62 of the General Statutes.

2. Tapoco is a duly organized public utility and is domesticated as such under the laws of North Carolina. It is subject to the jurisdiction of this Commission with respect to its retail rates and electric service as provided in Chapter 62 of the General Statutes.

3. Both Nantahala and Tapoco are wholly owned subsidiaries of Alcoa. Alcoa is a public utility pursuant to G.S. 62-3(23)c. and is subject to the jurisdiction of this Commission with respect to retail ratemaking.

4. The Nantahala and Tapoco electric facilities constitute a single, integrated electric system and are operated as such by, and as a coordinated part of, the Tennessee Valley Authority (TVA) system.

5. For purposes of setting the Applicant's rates in this proceeding the Nantahala and Tapoco systems should be treated as one entity with respect to all matters affecting the determination of the Applicant's reasonable cost of service applicable to its North Carolina retail operations.

6. The New Fontana Agreement (NFA), executed by TVA, Alcoa, Nantahala, and Tapoco, and the resultant 1971 Apportionment Agreement between Tapoco and Nantahala, have resulted in substantial benefits to Alcoa to the significant detriment of the customers of Nantahala.

7. The methodology employed by the Intervenors in making jurisdictional cost allocations and cost-of-service allocations is the most appropriate for use in this proceeding. Consequently, each finding of fact appearing in this Order which deals with the proper level of rate base, revenues, and expenses has been determined based upon said methodology.

8. The reasonable original cost of the Nantahala-Tapoco property used and useful in providing electric service to its retail customers in North Carolina is \$36,951,000. The reasonable accumulated provision for depreciation is \$18,202,000, and the reasonable original cost less depreciation is \$18,749,000.

9. The reasonable replacement cost of Nantahala's property used and useful in providing retail electric service in North Carolina is \$57,795,000.

10. The fair value of Nantahala-Tapoco's utility plant used and useful in providing electric service to its retail customers in North Carolina should be derived from giving 40% weighting to the original cost less depreciation of Nantahala-Tapoco's utility plant in service and 60% weighting to the trended original cost less depreciation of Nantahala-Tapoco's utility plant. By this method, using the depreciated original cost of \$18,749,000 and the reasonable replacement cost of \$57,795,000, this Commission finds that the fair value of said utility plant devoted to intrastate retail electric service in North Carolina is \$42,177,000. This fair value includes a reasonable fair value increment of \$23,428,000.

11. The reasonable allowance for working capital is \$1,113,000.

12. The fair value of Nantahala-Tapoco's plant in service used and useful in providing electric service to its retail customers within the State of North Carolina of \$42,177,000 plus the reasonable allowance for working capital of \$1,113,000 less customer deposits of \$188,000 yields a reasonable fair value of Nantahala-Tapoco's property in service to North Carolina retail customers of \$43,102,000.

13. The approximate gross revenues for the test year, after accounting and pro forma adjustments, under rates approved by Commission Order of June 14, 1977, are \$11,067,000.

14. The approximate level of test year operating expenses under rates approved by Commission Order of June 14, 1977, after accounting and pro forma adjustments, including taxes and interest on customer deposits, is \$8,322,000 which includes an amount of \$1,133,000 for actual investment currently consumed through reasonable actual depreciation after annualization to year-end levels.

15. The reasonable original cost capital structure for use herein is as follows:

Item	Percent
Debt	40.05
Common equity	37.00
Cost-free	22.95
Total	100.00

and when the fair value increment is added, the reasonable fair value capital structure becomes:

Item	Percent
Debt	18.28
Common equity	71.24
Cost-free	10.48
Total	100.00

16. The fair rate of return that Nantahala should have the opportunity to earn on the fair value of its investment de[illegible]ted to its North Carolina retail operations is 4.20%.

17. The approximate annual level of revenues which Nantahala should be authorized to collect through rates charged for its sales of service, based upon the findings of fact set forth hereinabove, is $9,032,000.

18. The rates and charges of Nantahala, based upon the adjusted test year level of operations, under rates approved by Commission Order of June 14, 1977, are excessive to the extent that said rates produce a level of revenue which is $2,035,000 ($11,067,000—$9,032,000) greater than the Applicant's revenue requirement (cost of service). Thus, Nantahala should be required to reduce said rates and charges in a manner so as to achieve an annual gross revenue reduction of approximately $2,035,000, based upon the adjusted test year level of operations.

19. Nantahala should be required to refund to its North Carolina retail customers all revenue collected under the rates approved by Commission Order issued June 14, 1977, to the extent that said rates produced revenue in excess of the rates approved herein. Said refund shall include revenues collected under the Company's base rate structure as well as through operation of the purchased power adjustment formula plus interest computed and compounded at the legal annual rate.

20. The purchased power adjustment clause is a just and reasonable rate and a reasonable method by which Nantahala can recover a part of its reasonable operating expense.

21. Alcoa has so dominated certain transactions and agreements affecting its wholly owned subsidiary Nantahala that Nantahala has been left but an empty shell, unable to act in its own self interest, let alone in the interest of its public utility customers

in North Carolina. Therefore, this Commission is compelled to order that, to the extent Nantahala is financially unable to make the revenue refunds required in this Order, Alcoa shall refund all or any portion of the aforementioned revenue refunds that Nantahala is financially unable to make.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 1

The evidence for this finding is contained in the verified Application and in the record as a whole. This finding is essentially procedural and jurisdictional in nature and is not contested.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 2 AND 3

The Commission Order of October 3, 1980, in this docket declared Tapoco and Alcoa to be public utilities in North Carolina and subject to the jurisdiction of the Commission. That Order, with its findings and conclusions and discussion of the evidence in support thereof, is attached hereto as Exhibit A and is incorporated into this Order by reference. The Commission concludes that Tapoco is a public utility and is subject to the jurisdiction of this Commission with respect to its retail rates and electric service. The Commission also concludes that Alcoa is a public utility pursuant to G.S. 62-3(23)c. and is subject to the jurisdiction of this Commission with respect to retail ratemaking.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 4 AND 5

In its opinion, *Utilities Commission* v. *Edmisten, Attorney General,* 299 NC 432, the Supreme Court stated, at page 435.

> "The transmission facilities of Nantahala and Tapoco are integrated and interconnected into a single system. . ."

And at pages 442 and 443, the Supreme Court further concluded that the Nantahala-Tapoco electrical system is a single system:

> "In light of the foregoing, we cannot agree with the Commission that the evidence is insufficient to warrant the treatment of Nantahala and Tapoco as a single system for rate making purposes. The 'roll-in' device, or technique, for rate making computation seems especially appropriate in a case such as this where one physically integrated system interconnected in such a way that all power available to the system can be used to enhance its overall reliability and supply its requirements as a whole, is presided over by two corporate entities (See, e.g., *Central Kansas Power Co.* v. *State Corporation Commission,* 221 Kan. 505, 561 P. 2d 779 (1977)). This is especially true when both corporate entities are wholly owned by a parent corporation which benefits from the power generated by the system. This device does nothing more than recognize that the two corporate entities ought, for rate making accounting purposes, be treated as the one electrical power producing and distribution system which, in fact, they are. If the then unlawful preferences are indeed accorded to Alcoa to the detriment of Nantahala's customers because of the separate corporate structures and the intercorporate apportionment agreements, this rate making device would seem to eliminate them. . . ."

These findings by the Supreme Court, that Nantahala and Tapoco constitute a single, integrated electric system and should be treated as one system for ratemaking purpose, have been carefully considered by the Commission for purposes of this proceeding. However, since Alcoa and Tapoco were not parties to the original proceeding that led to the June 14, 1977, Order, the Commission has allowed them and Nantahala to introduce evidence in the remand proceeding to challenge the findings of the Supreme Court. Notwithstanding the assertions of Mr. Vander Veen and other witnesses for the respondents that the Court's decision was based on the "misconception" that Nantahala and Tapoco are a single, unified system, the evidence presented in the

remand proceeding strongly reinforces the Supreme Court's determination in this regard. The evidence is overwhelming and undisputed that Nantahala and Tapoco are both wholly owned by one corporate parent, Alcoa. The facilities of Nantahala and Tapoco are located in contiguous areas in western North Carolina. The Nantahala and Tapoco electric facilities are physically interconnected with each other, and both companies are interconnected with TVA; power can be dispatched and transmitted from the facilities of one to the facilities of the other. The original Fontana and the New Fontana Agreements treat the facilities of Nantahala and Tapoco without discrimination and make them an integrated part of, and subject them to coordination by, the TVA system. By the terms of these agreements TVA receives the output of all of the hydro resources of both Nantahala and Tapoco, except for three small projects of Nantahala. By terms of these agreements Tapoco and Nantahala also turn over to TVA control of production and stream flow. Accordingly, TVA determines for Tapoco and Nantahala, as a single entity, both electric generation and stream flow and operates them as a coordinated system as a part of TVA's own system. In turn, Tapoco and Nantahala jointly receive back from TVA certain entitlements of power which they divide between themselves by the 1971 Nantahala-Tapoco Apportionment Agreement.

Intervenors' witness Springs testified that it is a "false and arbitrary assumption that NP&L and Tapoco operate as isolated systems when in fact they do not." When witness Springs was asked whether the Nantahala and Tapoco facilities should each be operated as a separate and independent system, he replied: "No, by coordinating them as one system with TVA, the outputs of the generating resources are maximized." (Tr. Vol. 15, p. 50) Witness Springs also testified that, from an engineering standpoint, the Nantahala and Tapoco facilities should be operated as one utility.

The Commission concludes that the Nantahala and Tapoco electric facilities constitute a single, integrated electric system and are operated as such by, and as a coordinated part of, the TVA system.

The Commission also concludes that, for purposes of setting Nantahala's rates in this proceeding, the Nantahala and Tapoco systems should be treated as one entity with respect to all matters affecting the determination of Nantahala's reasonable cost of service applicable to its North Carolina retail operations. Elsewhere in this Order the Commission has made findings and conclusions determining that a roll-in of Tapoco together with Nantahala for rate-making purposes will result in a significant reduction in the cost of providing public utility electric service to the customers of the combined Nantahala-Tapoco system. The Commission incorporates those findings and conclusions herein.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 6 AND 7

The Commission, as previously discussed, has determined for purposes of this proceeding that the Nantahala and Tapoco systems should be treated as one entity. The Commission must now determine the proper allocation methodology to be used in apportioning the combined revenues, expenses, and investment of the Nantahala-Tapoco system between that applicable to said system's North Carolina retail operations and that applicable to said system's operations over which this Commission has no jurisdiction.

Generally speaking, the allocation methodology that the companies (Alcoa, Tapoco) would have the Commission adopt for use herein is based in all material respects upon demand and energy entitlements as described and set forth in the New Fontana Agreement and the Tapoco-Nantahala Apportionment Agreement; whereas, the allocation methodology that the Intervenors

would have the Commission adopt is based in all material respects upon the assumption that the electric energy requirements of the Nantahala-Tapoco combined system's North Carolina public load has first call on the total electric energy output of the combined system, and to the extent that said output exceeds the requirements of the North Carolina public load, such excess will be available for sale and will be purchased by Alcoa. The Commission will first address the propriety or, perhaps more appropriately, the impropriety of basing cost allocations on demand and energy entitlements as contained in the New Fontana Agreement and the Tapoco-Nantahala Apportionment Agreement.

There are a number of inequities to Nantahala that arise out of both the New Fontana Agreement (hereafter NFA) and the 1971 Tapoco-Nantahala Apportionment Agreement (hereafter Apportionment Agreement) that result in Alcoa's receiving concealed benefits. Because the inequities of the NFA are more subtle and difficult to express than are those of the Apportionment Agreement, we discuss the 1971 Apportionment Agreement first.

A. *Concealed Benefits of the Apportionment Agreement*

(1) Quantity of Nantahala's Production

Alcoa's power consultant George Popovich devised the Apportionment Agreement share for Nantahala at 360 million Kwh annually. Nine years earlier, Mr. Popovich had determined that a considerably higher apportionment share would be required for Nantahala. On May 14, 1962, in a memo to an Alcoa executive, Mr. Popovich wrote:

> "A. The Alcoa-NP&L Co. Contract of October 1954 as verbally revised should guarantee that the annual energy entitlements of NP&L Co. are 360 million Kwh (41,000 Kw) primary and 79 million Kwh (9,000 Kw) interruptible. This is a benefit in that it gives NP&L Co. this assured supply even in the event of future conditions of stream flow which

might be more adverse than that experienced in the historical period of record. These energy entitlements have been independently determined by engineers employed by NP&L Co. Alcoa has checked and accepted their determinations. . . ." (underlining supplied) (Intervenors Popovich Rebuttal Cross-Examination Ex. 1, pp. 3–4)

The engineering study referred to by Mr. Popovich had been made by Ebasco in the year 1960 and a copy of that study is Item 4, A.G. Jontz Cross-Examination Exhibit 1 (original hearing). That study states:

"(a) The primary energy capability under the most adverse water conditions of record. This quantity was found to be 360 million kilowatt hours per year.

"(b) The average energy that could be generated annually by these hydroelectric plants. This quantity was found to be 439 million kilowatt hours per year."

We note that the 79,000,000 Kwh referred to by Mr. Popovich as interruptible is the difference between primary and average energy referred to in the Ebasco study. (When the three small Nantahala plants not included in the NFA return entitlement from TVA are deducted, the 79,000,000 Kwh is reduced to 66,000,000 Kwh.)

Based upon these established and known facts, after the NFA was executed, in 1963 Alcoa entered into a written agreement with Nantahala wherein Nantahala was apportioned a certain share of the NFA return entitlements. This agreement, identified as Item 35, Truett, et al., Judicial Notice Ex. 1 (original hearing), and also Applicant's Exhibit WMJ-R11, apportioned to Nantahala 360,000,000 Kwh minimum plus actual production in excess of 360,000,000 Kwh, that is, an average of 426,000,000

Kwh annually (360,000,000 Kwh + 66,000,000 Kwh), using this language:

"2. Nantahala should be entitled each month to an amount of energy which when added to its generation at plants not operated under the above mentioned agreement of December 27, 1962, shall be the equivalent either to its total actual generation during that month or to the one-twelfth of its annual primary generating capability whichever shall be the greater. The annual primary generating capability of Nantahala as used in the foregoing sentence is agreed to be 360 million kilowatt hours."

By this agreement, Nantahala received annually the average of 426,000,000 Kwh, of which 360,000,000 Kwh was guaranteed as a minimum.

During the remanded hearings, Intervenors put on similar independent evidence from their expert witness Springs. Witness Springs testified, at Vol. 15, Tr. p. 33:

". . . NP&L's contributions, excluding the three small projects not turned over to TVA, are approximately . . . 426,000,000 Kwh of average energy (Ebasco Study) . . ."

Despite all of the above facts, when Mr. Popovich devised the 1971 Apportionment Agreement, Nantahala received *only* 360,000,000 Kwh annually. Nantahala was deprived of an average of 66,000,000 Kwh annually. The detriment to Nantahala constitutes a benefit to Tapoco that is passed on to Alcoa.

Witness Springs testified that "NP&L did not come out very well in this 'trade.'" (Vol. 15, Tr. p. 19)

(2) Quantity of Nantahala's Peaking Capacity

As one aspect of the 1971 Apportionment Agreement, Nantahala has a limitation placed upon its peaking capacity of 54,300 Kw with the result that any time it has to provide a customer

demand in excess of 54,300 Kw, it must pay a monthly demand charge to TVA for all power over that limitation. If the limitation were at a higher level, of 81,800 kilowatts, a monthly demand charge would be saved for 27,500 kilowatts, i.e., the difference between 81,000 Kw and 54,300 Kw, when customer demand equalled or exceeded the 81,000 kilowatt level.

Demand costs imposed on Nantahala for use of capacity between its assigned capacity of 54,300 kilowatts and its actual capacity, of 81,800 kilowatts, would represent an expense to Nantahala and, thus, a savings to its New Fontana Agreement sister, Tapoco, since the capacity constraints for the TVA return entitlements are jointly shared by them under the New Fontana Agreement. Tapoco's savings are passed on to Alcoa so as to become Alcoa savings, i.e., a concealed benefit.

The record clearly and convincingly establishes that Nantahala's correct capacity is 81,800 kilowatts and that, by being assigned a demand limitation of only 54,300 kilowatts, Nantahala suffers significant monthly financial loss.

The 1960 Ebasco Study (Item 4, A.G. Jontz Cross-Exam Ex. 1, Table A-1, (original hearing)), undertaken for Nantahala by independent experts, computed Nantahala's plant capacity, under the most adverse water conditions, at 85,400 kilowatts. After deducting the three small plants excluded from the NFA, that capacity is 84,300 kilowatts (Vol. 15, pp. 147–148). The Ebasco study computation is confirmed in an old memorandum of W.T. Walker (Intervenors' Ex. DAS-18, pp. 4–5 of 8), Nantahala's president, wherein he notes that in 1965 another independent source had analyzed Nantahala's *allowed capacity* under the original Fontana Agreement to be only 35,172 kilowatts. Not only was the allowed capacity under the original Fontana Agreement regarded as unrealistic, but a capacity much higher

than 54,300 Kw was thought to be proper. The Walker memorandum states:

> "... He thought this allocated capacity to be unreasonable for a company with 84.3 Mw of co-ordinated capacity under adverse water conditions, so he allocated 74.9 Mw to Nantahala ..."

The Walker memorandum continues, at page 5 of 8, by even noting that "George Popovich's proposed allocation to Nantahala ..." for capacity would be 76,000 Kw.

Based upon these established facts, after the NFA was executed, Alcoa entered a written agreement with Nantahala in the year 1963 wherein Nantahala was allowed to use capacity without limitation. This agreement, mentioned in the previous section, identified as Item 35, Truett, et al., Judicial Notice Ex. 1 (original hearing) and also Applicant's Ex. WMJ-R11, thereby permitted Nantahala to use actual capacity to the limits assigned by the 1960 Ebasco study.

Intervenors' witness Springs testified that after adjustment for reserves, the allowable capacity of 84,300 kilowatts, under most adverse water conditions, should be 81,800 kilowatts (Vol. 15, Tr. p. 37).

Despite these impressive studies and facts, when Mr. Popovich accomplished his study (Intervenors' Ex. DAS-12) for the 1971 Apportionment Agreement, while accepting the most adverse water capacity factor of 84,300 kilowatts, he deducted 27,500 kilowatts for the "largest unit out" to reach an assigned capacity of 54,300 Kw. This deduction is for the Nantahala facility which forms upwards of 50% of the entire Nantahala generation system of 11 dams.

If Nantahala were a separate and independent system, a deduction of the "largest unit out" might be appropriate to determine assured capacity. However, Nantahala is not and never has

been a separate electric system—it was not so designed. Nantahala's two largest facilities are Thorpe (previously Glenville), completed in 1941 with 21,600 Kw capacity, and Nantahala, completed in 1942 with 43,200 Kw capacity (See Intervenors' Ex. DAS-1, p. 8 of 14). The Thorpe and Nantahala facilities comprise about 65% of Nantahala's entire system. At the time of their construction, Alcoa obtained a certificate of necessity from the War Department and *expressly argued and avowed that they were part of the Alcoa system.* Intervenors' Ex. DAS-7, p. 5 of 11; also being Applicant's Ex. WMJ-R5. In that exhibit, at pp. 5-6 of 11, it is recorded that Alcoa said of these two Nantahala plants:

> "At the present time, Alcoa receives power from three dams located on tributary waters of the Tennessee River at Calderwood, Tennessee and Tapoco, North Carolina, (Cheoan and Santeetlah developments). . . .
>
> "To improve the present power situation and to supply a portion of the 200,000 additional Kw required for national defense purposes, *applicant proposes to build two new developments,* also on tributaries of the Tennessee River, at Glenville and Nantahala, North Carolina . . . *The estimated total addition to the Alcoa power system* is 51,500 Kw, part of which will be produced at the new developments and part from additional water released for us downstream." (emphasis added) (Apparently, the two new projects were finally designed for their actual greater combined capacity, 64,800 Kw.)

Furthermore, for the past 40 years, both Nantahala and Tapoco have been operated as an integral part of the TVA electric system pursuant to the provisions of the Fontana and New Fontana Agreements. Moreover, when Alcoa negotiated these agreements with TVA, it did not bargain for return power from TVA as if Nantahala was an independent power system but rather the attributes of the Alcoa system were melded together with the TVA system for evaluation purposes. In this regard, Intervenors' Ex. DAS-23 is a memorandum of Alcoa's meetings with TVA respecting negotiations for the NFA wherein the TVA proposals were based on integration into and coordination with the TVA system (Intervenors' Ex. DAS-23, pp. 6-7 of 85).

With Nantahala and Tapoco being thus integrated into and coordinated with the TVA system, it is not appropriate to determine Nantahala's assured capacity by configuring Nantahala as a single independent and isolated system and to use the "largest unit out" methodology. Instead, Nantahala should be treated as part of the TVA system and the reserve margin used by TVA should be applied. TVA does not use a reserve of "largest unit out" but rather uses "the loss of load probability method." (See Intervenors' Ex. DAS-13, p. 1 of 3). Due to the favorable operating characteristics of a hydro system as opposed to a steam system, those characteristics being, for instance, low operating speeds, ruggedly constructed equipment, and restarting capability without auxiliary power, the reserve requirements of a hydro system are very low. Intervenors' Ex. DAS-17, being a portion of the 1980 contract of the Southern Company Services Intercompany Interchange, at page 6 of 6, shows that a 3% hydro reserve is proper.

Using a 3% reserve in place of the "largest unit out" reserve, in this case upwards of 50%, would establish a capacity under most adverse water conditions of 81,800 kilowatts as opposed to Mr. Popovich's calculation of 54,300 kilowatts. This is what Intervenors' witness Springs testified the calculation should be (Vol. 15, Tr. p. 37).

Significant cost is shifted to Nantahala by the unfair and unwarranted limitation of capacity to 54,300 kilowatts. Conversely, that expense, in the form of demand charges paid to TVA, is a concealed benefit to Alcoa.

(3) Nantahala's Upstream Benefits

Nantahala's projects are upstream of Tapoco's projects, except Santeetlah. As a consequence, water that is stored by Nantahala

can be released to flow downstream and be used by Tapoco for production of electricity. Therefore, Nantahala's storage has a value to Tapoco. Granted TVA's Fontana project now lies between the Nantahala and Tapoco projects. However, that does not diminish the value of Nantahala's stored water to Tapoco since, when Nantahala releases water, that water, or its equivalent, can be released by Fontana so as to flow through to Tapoco.

On January 10, 1941, before Fontana was constructed and even before the Fontana Agreement, Nantahala applied to the War Department for a certificate to build the Glenville (now Thorpe) and Nantahala projects, noting that they would be upstream of the Calderwood and Cheoah dams. That application, Intervenors' Ex. DAS-7, at p. 5 of 11, in part, makes this statement about the upstream benefits:

> " . . . It is contemplated that they will store water during the winter months, and will be used in the dry season to produce additional power and also to make available additional water for the developments downsteam . . . "

A 1956 TVA study estimated the upstream storage benefits of the two major Nantahala projects to Tapoco's downstream facilities. As shown by Intervenors' Ex. DAS-9, the Nantahala and Thorpe projects yield a *continuous* relative contribution to Tapoco's Calderwood and Cheoah projects of 4,300 Kw. This is the equivalent of 37,668,000 Kwh annually as an upstream benefit from Nantahala to Tapoco (4,300 × 8,760).

Despite the presence of Nantahala's upstream benefits to Tapoco, when Mr. Popovich devised the 1971 Apportionment Agreement, Nantahala received no credit for this benefit. Of course, the benefit accrued to Tapoco who passed the concealed benefit on to Alcoa.

(4) Nantahala's Entitlement for Operating Its Properties in Accordance with the Fontana Agreement

By the 1941 Fontana Agreement, Nantahala, at the instance of Alcoa, gave to TVA the right, *in perpetuity*, to control the storage and flow of water from its several hydroelectric projects. (See, Item 8, A.G. Popovich Cross-Examination Ex. 3 (original hearing)). Respecting the value of this right, the Fontana Agreement, at page 3, in part, states:

> "Whereas, the most efficient and economical operation of the hydroelectric plants on the Tennessee River and the Little Tennessee River and their tributaries requires the closely coordinated operation of the system of Authority (sic, TVA) with Company's (sic, Nantahala & Tapoco) plants, and such coordinated operation will make possible substantial benefits and economies; and
>
> "Whereas, operation under the provisions of this agreement will aid in the control of floods, the promotion of navigation, and the conservation of stored water; and . . . "

Unquestionably, Nantahala's giving up of rights constituted a loss of considerable value for which loss Nantahala has been entitled to compensation.

With the 1963 apportionment agreement between Alcoa and Nantahala (Item 35, Truett, et al., Judicial Notice Ex. 1 (original hearing), being also Exhibit WMJ-R11), Alcoa agreed to continue to pay to Nantahala monies for Nantahala's loss of those operational rights. Moreover, the agreement clearly stated that TVA was continuing to pay value for those rights, which value is reflected in the TVA return entitlement of the New Fontana Agreement. The 1963 Alcoa-Nantahala Apportionment Agreement at pages 1-2, in part, states:

> "Whereas, the agreement dated August 14, 1941, known as the 'Fontana Agreement' has been superseded in certain respects by a new agreement dated December 27, 1962; and
>
> "Whereas, heretofore Nantahala has received certain payments which represented payments to Nantahala from operating its properties in accordance with the terms of the Fontana Agreement; and

"Whereas, the above-mentioned agreement of December 27, 1962, (sic, NFA) was entered with the understanding among Nantahala, Alcoa and Tapoco, Inc. (a) that the benefits accruing to Nantahala thereunder would include the right to continue to receive payments equal in amount to the above-mentioned payments . . . "

"*Now, therefore*, it is agreed that during the term of the above-mentioned agreement of December 27, 1962:

"1. Alcoa shall pay Nantahala in monthly installments the sum of $89,200 per annum, which amount shall be in addition to the amounts otherwise paid by Alcoa to Nantahala for energy under such power purchase contract as shall be in effect from time to time."

Intervenors' witness Springs testifying on another aspect of this case, used language that is most appropriate to explain this matter:

". . . Thus, the Original Fontana Agreement still continues to confer significant benefits on Alcoa . . ." (Vol. 15, Tr. p. 27).

In the year 1963, in Docket No. E-13, Sub 13, the North Carolina Utilities Commission found the following facts concerning the TVA return entitlement as including a reimbursement to Nantahala. In Item 36, Applicant's Judicial Notice Exhibit (original hearing), at page 8, the Commission stated:

". . . The Evidence offered by Nantahala further disclosed that Nantahala operates under a working agreement between its parent, Alcoa, and TVA (the Fontana Agreement), wherein TVA exercises control of water release in the Nantahala generating system. For this privilege, TVA delivers to Alcoa approximately 25,600,000 Kwh at 100 percent load factor (compensation power) for the credit of Nantahala . . ."

At page 8, the Commission further stated:

"7. Alcoa pays Nantahala for TVA's control of the release of water in Nantahala's generating system at the rate of 3.5 mills per Kwh, based on 25,600,000 Kwh annually. This payment is below the rate paid by Alcoa to Nantahala for firm power."

Despite the fact that the NFA includes in the TVA return entitlement a reimbursement by TVA for the right to operate Nantahala's projects for which Alcoa previously paid $89,200 annually to Nantahala, when Mr. Popovich devised the 1971 Apportionment Agreement he gave no credit to Nantahala for that entitlement.

Under the terms of the 1971 Apportionment Agreement, Nantahala receives neither an energy credit nor a monetary payment for the right given up. Naturally, since the TVA payment for the operational rights, which is paid with energy in the NFA rate entitlement, did not go to Nantahala, it inured to the benefit of Tapoco. In turn, Tapoco passes this concealed benefit to Alcoa. (It should be noted that 3.5 mills has, for many years, constituted far less than the present value of electric energy.)

(5) Nantahala's Value to the TVA Interconnected System

Another failure of the Apportionment Agreement respecting Nantahala's participation is that the Popovich formula does not consider the proper value to Nantahala of the fact that the Nantahala, Tapoco, and TVA systems are interconnected. Interconnection is of considerable value to TVA completely aside from the fact that Nantahala's rate base includes in it certain assets devoted to the interconnection, which assets are entitled to earn a rate of return. Because Nantahala is not an isolated system, it should be receiving the usual benefits that accrue from coordinated operation. Yet, Nantahala does not receive the usual benefits of an interconnected and coordinated system.

Intervenors' Exhibit DAS-23 consists of many pages of Alcoa memoranda reflecting the path of negotiation between Alcoa and TVA for the New Fontana Agreement. While there are several

references to the matter of interconnection, we refer only to a few which illustrate that interconnection has considerable value. At page 28 of 85, one memorandum says:

> ". . . Copies of our studies were given to TVA and they showed that the new TVA proposal could be supplied from our present system without any apparent consideration given to gains that TVA will realize from integration and the peaking capacity on our system.
>
> "As mentioned above, TVA will check our studies on their own computer and if these studies are confirmed, we will have immediate discussions in an effort to determine what studies should be made to properly determine the benefits of integration, use of our peaking, etc. . ."

Again, on page 30 of 85, Intervenors' Exhibit DAS-23, an Alcoa memorandum states:

> "II. *We do not believe present TVA proposal equitable because*:
>
> a. Our system will alone produce the TVA proposal. . . . We argued, however, that TVA could realize advantages of integration, peaking, etc., and still provide their proposal to us from our system."

Again, on page 34 of 85 of Intervenors' Exhibit DAS-23, another Alcoa memorandum states:

> "There is a strong feeling among the Engineering Department, particularly Messrs. Gnuse, Tompkins, Eagleton, Popovich and others, that the value to TVA of integrated operation is much greater in 1960 than it was in 1941 at the time the contract was negotiated. They have argued that because of this, TVA should be willing to renegotiate the entire Fontana Agreement recognizing the present inequities. . . ."

Of course, during further negotiations, Alcoa was able to derive considerable gain from TVA for the integrated systems factor. We have previously mentioned certain benefits of a coordinated,

integrated operation, such as the need for smaller reserves and, in this case, that TVA actually controls production of generation and storage waters.

However, we have not mentioned the value in integration of Nantahala's projects that are upstream of TVA's Fontana Project. In an integrated system such value is maximized. Since the Fontana Project is located below Nantahala's projects (See Intervenors' Ex. DAS-3) and above the Tapoco projects, other than Santeetlah, the Fontana Project receives the benefit of the storage capability of the Nantahala projects. Indeed, the TVA Tennessee River system receives the benefit of the storage of all of these projects located on the Little Tennessee River system. This is especially true since, under the New Fontana Agreement, TVA has control of all of these reservoirs on the Little Tennessee River system, except the three small projects of Nantahala which are not included. Intervenors' Ex. DAS-9 shows the results of a TVA study of downstream storage benefits. According to this study, the Nantahala and Thorpe units alone added 12,400 Kw of continuous primary power to the TVA system. This is equal to 108,624,000 Kwh per year (12,400 x 8,760 hours) (Vol. 15, Springs pp. 48–49). We have already considered that the upstream Nantahala and Thorpe projects yield a continuous relative contribution to Tapoco's Calderwood and Checah projects of 4,300 Kw, which is 37,668,000 Kwh annually. This benefit to Tapoco should be deducted from Nantahala's total upstream benefit of 108,624,000 Kwh in order to obtain Nantahala's upstream benefit to TVA. After deduction, Nantahala's annual upstream benefit to TVA is calculated to be 70,956,000 Kwh.

Examination of the NFA reveals that the parties cancelled out their respective upstream benefits when that bargain was struck. Since Nantahala provided benefits upstream to both TVA and Tapoco, and TVA provided benefits upstream to Tapoco, it was Tapoco which gained by that mutual cancellation. Certainly, Nantahala lost the benefit of the value of 70,956,000 Kwh

annually. Surely, Nantahala should receive in a joint agreement with TVA the benefit of that integrated upstream storage.

When the 1971 Apportionment Agreement was entered into between Tapoco and Nantahala, Tapoco should have been willing for Nantahala to have an additional 70,956,000 Kwh annually assigned to it as the value of integrated storage, but when Mr. Popovich devised the apportionment formula Nantahala got no such benefit. As a consequence, to Tapoco's benefit, Nantahala was deprived of one value of the interconnection with the TVA system. This concealed benefit flowing from Nantahala to Tapoco is, of course, passed on by Tapoco to Alcoa.

(6) Summary of Detriment to Nantahala from the 1971 Apportionment Agreement

By the 1971 Apportionment Agreement, Nantahala was given no credit for the following:

1. Average production in excess of primary production	66,000,000 Kwh annually
2. Benefits upstream of Tapoco	37,668,000 Kwh annually
3. Entitlement for operating properties under Fontana Agreement	25,600,000 Kwh annually
4. Value to TVA of the interconnected system	70,956,000 Kwh annually
	200,224,000 Kwh annually

In addition, Nantahala received no credit for its peaking capacity of 27,500 kilowatts over the 54,300 kilowatts assigned to it, for which Nantahala must pay demand charges to TVA when monthly demand exceeds assigned capacity.

The North Carolina Supreme Court, in *Edmisten, supra*, at pages 440–441, when considering just the failure of Nantahala to receive benefit for its average production, stated:

> "... Suffice it to say that the assertion that Nantahala's public is fairly served by a contract requiring Nantahala to purchase additional power regardless of the adequacy of its own generation *assaults the common sense of this Court* . . ." (emphasis added)

Now that considerably more of the various detriments to Nantahala have been exposed and fleshed out, it is apparent that the 1971 Apportionment Agreement works an extensive injustice on Nantahala and its public ratepayers, the gravity of which far exceeds even that envisioned by the Supreme Court.

B. *Concealed Benefits of the New Fontana Agreement*

The concealed benefits flowing from Nantahala to Alcoa by virtue of the New Fontana Agreement are entirely different from those previously discussed which flow from the 1971 Tapoco-Nantahala Apportionment Agreement. The basic inequity to Nantahala arising out of the NFA is that the energy entitlement returned to Nantahala and Tapoco from TVA is structured to meet Alcoa's demand for a certain amount of stable electricity for purposes of aluminum production rather than a demand for a public load. Consequently, the NFA returns an average of 218,300 kilowatts of energy at a high load factor with minimal peaking deviation, which load is principally designed to service Alcoa's pot-lines and other production electrical requirements. Even the interruptible and curtailable energy entitlement returned to Tapoco-Nantahala is in increments of wattage that conform to the demands of a pot-line so that, if power is interrupted or curtailed, Alcoa can respond by cutting out a particular pot-line.

Nantahala, on the other hand, has a fluctuating demand for energy which has peaks and valleys. This is typical of a public service load. Nantahala's electrical requirement is for assured, but

constantly, variable amounts. Nantahala needs peaking capacity and its generation projects possess peaking capacity, yet the NFA traded away that peaking capacity to TVA. The Intervenors urge that it would be ridiculous, as a result of enlightened, arm's-length bargaining, to turn over Nantahala's peaking capacity to TVA and then, at such time as its load requires peaking capacity, to buy that same capacity back from TVA at a very high price. The Commission agrees that the detriment resulting to Nantahala from the design of NFA flows to Alcoa as a benefit.

Intervenors' witness Springs testified as to the details of Alcoa's concealed benefits derived under the NFA (Vol. 15, Tr. pp. 39–46). He showed that Alcoa reaped enormous benefits through the improvement of the availability of Tapoco's secondary energy production *from* a level of 42% *average curtailment to an average curtailment* rate of only 8% (Vol. 15, Tr. pp. 39–40).

He also showed that the Tapoco generation statistics reflect the coordination of the Fontana Project and other forms of integration with TVA, which are inconsistent with the isolated system model utilized as the basis for the 1971 apportionment study (Vol. 15, Tr. pp. 43–44). As stated in a memorandum by George Popovich contemporaneously with the negotiation of the NFA:

> "It is my opinion that, to Alcoa, the present proposal (sic, NFA) represents an improvement over the existing Fontana Agreement. In day years this improvement could be substantial . . ." (Ex. DAS 23, p. 59 of 85)

Alcoa was in direct control of the negotiations, and, unlike the Nantahala ratepayers, has had every ability to protect its own interests during the negotiations (Vol. 15, Tr. p. 46–47). Respondents cannot now be heard to claim that they are dissatisfied with the NFA so as to place the cost responsibility for the deficiencies of that agreement upon Nantahala's ratepayers.

One reason the NFA may have been designed so exclusively to meet Alcoa's needs, to Nantahala's detriment, was because when the NFA negotiations were underway, the parties contemplated

the sale of Nantahala's distribution system to Duke. By the sale to Duke, Nantahala would have been left with its generation but would have been without a public service load. Nantahala would then have taken its NFA entitlement and delivered it all to Alcoa. Accordingly, the power Nantahala would have gotten under the NFA would have been satisfactory for delivery to Alcoa irrespective of quantity and design.

A sale of Nantahala's distribution system to Duke had been approved by the North Carolina Utilities Commission and the approval Order, in turn, had been approved by the Superior Court. It was not until the year 1963 that the Supreme Court stopped the sale, which date was after the New Fontana Agreement had been executed. See *Utilities Commission* v. *Membership Corp.*, 260 N.C. 59, 131 SE 2d 865 (1963). Prior to the Supreme Court's action, Alcoa personnel had believed that the sale to Duke was to be approved. Thus, in an Alcoa memorandum dated May 27, 1960, being Intervenors' Ex. DAS-23, p. 2 of 85, it is recorded:

> ". . . They (sic TVA) asked us the status of the sale of Nantahala to Duke. We told them that the matter was at a standstill at the present time but we were continuing our efforts to complete the transaction and we expected that the sale would take place perhaps within the next year . . ."

In a memorandum of August 23, 1960, being page 15 of 85 of Intervenors' Ex. DAS-23, it is stated:

> "One final note, the entire TVA proposal is based upon the sale of the Nantahala Power Company. TVA proposed that if the sale was not complete at the time this new proposed contract becomes effective, they would increase the power available to us under the purchase contract to whatever amount is necessary for us to handle the Nantahala peak. This would be done on a temporary basis and would be reduced concurrent with the transfer of the Nantahala properties to Duke."

In another memorandum of November 6, 1962, being Intervenors' Ex. DAS-23, p. 83 of 85, which is the final memorandum

after completion of all negotiations for the NFA, the following is written:

> "... In my opinion it will be preferable for us to sell the Mission Plant to TVA whenever we transfer the Nantahala properties to Duke ..."

These memoranda clearly establish that during the entire 2½ year period over which the NFA was negotiated between TVA and Alcoa, both parties contemplated that Nantahala's entire public service load would be sold to Duke. Based on this assumption, the entire TVA return entitlement to Alcoa was structured in such a manner as to meet Alcoa's load requirements for aluminum production. In no manner was the NFA structured to meet Nantahala's needs (Vol. 15, Tr. p. 47). We support this obvious conclusion even further by noting that on January 1, 1963, five days after the signing of the NFA, Alcoa and Nantahala executed an agreement between themselves to reflect "understandings" made between the affiliated companies at the time of the signing of the NFA. In this agreement, being Item 35, Truett, et al., Judicial Notice Ex. 1, also being Applicant's Exhibit WMJ-F 11, it was stated:

> "Whereas, the above-mentioned agreement of December 27, 1962 was entered into with the understanding among Nantahala, Alcoa and Tapoco, Inc. (a) that the benefits accruing to Nantahala thereunder would include the right to continue to receive payments equal in amount to the above-mentioned payments and, in addition, the right each month to an amount of energy which, together with its generation at plants not under said agreement, would be equivalent to its total acutal generation but in no event less than one-twelfth of its annual primary generating capability, and (b) that certain obligations and benefits thereunder would be performed and enjoyed as herein set forth ..."

The significance of this latter agreement is that since the NFA was obviously structured to Alcoa's need rather than to Nantahala's, Alcoa and Nantahala agreed that Nantahala could

obtain certain power entitlements from the TVA return and, additionally, receive other monetary benefits from Alcoa.

Also, Intervenors' expert witness Springs testified, in part, as follows:

> "Throughout the negotiations, TVA and Alcoa had every reason to assume that NP&L's distribution system would soon be sold off to Duke Power Company. NP&L did not even have a representative at any of the negotiating sessions. Alcoa secured the benefits of being integrated with TVA, including the benefit of storage releases from Fontana which are *vital to the operating of Tapoco's facilities.* ... The 1963 Apportionment Contract shows in its face that the New Fontana Agreement was never intended as a 20-year power supply for NP&L public load. It appears that NP&L's officers and consultants were primarily concerned with the effect of the Agreement on the ongoing rate case and transfer cases before the NCUC and not with the interest of NP&L ratepayers over the 20-year period of Agreement." (emphasis added) (Vol. 15, Tr. p. 47)

The foregoing evidence of record clearly demonstrates that the NFA was tailored to meet Alcoa's aluminum production needs without consideration of Nantahala's public service needs, that the NFA return entitlement from TVA is not suitable for Nantahala's operations (although it is very suitable for aluminum production) and that Nantahala's participation in the TVA return entitlement could not be secured without a monetary supplement from Alcoa to Nantahala. The Intervenors have not established how much better Nantahala would have fared if the NFA had been negotiated for a TVA return suitable for servicing a public load, nor have they attempted to do so. Such proof is unnecessary. It is too hypothetical to conjecture as to what quantum and type of return energy Nantahala should have negotiated for and as to what TVA would have been willing to agree upon. Nantahala was not designed as, and is not in reality, a separate

utility system but, rather, is part of an integrated Alcoa system with Tapoco. As expert engineering witness Springs testified:

> ". . . I agree with a rolled-in-cost-of-service approach for NP&L and Tapoco, because it is impossible to separate out the functional relationship between the generating resources operated by these companies and the load they each serve." (Vol. 15, Tr. p. 56)

Summarizing the foregoing inequities to Nantahala which result from the New Fontana Agreement, it can be stated that the TVA return entitlement was entirely designed for Alcoa's industrial load and was not suitable for Nantahala's public service responsibilities. Nantahala needed peaking capacity and had peaking capacity from its own generating stations, yet Nantahala gave up that capacity with the result that it must buy high cost power from TVA to meet its peaking responsibilities. The extra costs thus incurred by Nantahala inure to the benefit of Alcoa. For instance, by the 1963 Alcoa-Nantahala Apportionment Agreement, even Alcoa recognized, in fact, the unfairness to Nantahala produced by the NFA and agreed to pay an annual cash settlement of $89,200, to Nantahala to offset some of the inequities.

Any regulatory reformation of the NFA to properly award to Nantahala its just entitlements would, of necessity, be somewhat hypothetical. At this late stage of the case, and particularly with an alternative solution available, such reformation should not be attempted. The roll-in technique avoids the need for complete identification of inequities and is nicely suited as a proper alternative to reformation of contracts. The Supreme Court, in *Edmisten, supra,* at p. 443, called for use of the roll-in in this case, if beneficial to the public, with this language:

> ". . . This device does nothing more than recognize that the two corporate entities ought, for rate making accounting purposes, be treated as the one electrical power producing and distribution system which, in fact, they are. If then unlawful preferences are indeed accorded to Alcoa to the detriment of Nantahala's customers because of the separate corporate structures and the inter-corporate apportionment agreements, this rate making device would seem to eliminate them. . . . The case is remanded with directions to the Commission to obtain and consider information and data showing what Nantahala's cost of service to its customers would be if this method of rate making were used and whether Nantahala's customers would benefit thereby."

Further, the Commission notes that while Nantahala's facilities were obligated as provided under the Original Fontana Agreement, it was not even permitted to be a signatory thereto. Even though it was a signatory to the New Fontana Agreement, it did not participate in the negotiations of that agreement. Moreover, Nantahala's employment contract with its president, William M. Jontz, provides, in pertinent part:

"*Section 2. Duties and Responsibilities.* Employee is hereby employed by Nantahala as Chief Executive Officer of Nantahala and shall act in such capacities pursuant to the supervision and direction of the Board of Directors of Nantahala (hereinafter sometimes referred to as the 'Board'). Major general objectives of such employment during the term hereof are for the Employee to:

> (a) Manage Nantahala as a public electric utility, within the restraints of regulatory controls, so as to achieve a profitability consistent with other public electric utilities in North Carolina.
>
> (b) Develop plans for the possible sale or other disposition of Nantahala and execute such plans should the Board of Directors of Nantahala so direct.
>
> (c) Accomplish (a) and (b) above so that there is little or no adverse impact on the operations and assets of Nantahala's parent company, Aluminum Company of America, and its subsidiaries in North Carolina, including, but not limited to, the generation and transmission of electric power by Tapoco, Inc. and Yadkin, Inc. and the operations of the Badin Works of Aluminum Company of America."

* * * * *

"*Section 3. Compensation.* For the performance on his duties and responsibilities, Employee shall receive the following compensation:

> (a) *Base Salary* . . . (NOTE: this subparagraph is not further here quoted, but it provided for probable annual achievement awards.)
>
> (b) *Achievement Award* To be determined annually by the three-member Aluminum Company of America group among the Board of Directors of Nantahala and to be based on the performance of Employee in reference to the major general objectives set forth in Section 2 hereof. The probable annual achievement awards for the respective contract years are set forth above."

* * * * *

"*Section 6. Nondisclosure.* . . . Nor shall Employee in any manner, directly or indirectly, aid or be a party to any act, the effect of which would tend to divert, diminish or prejudice the good will or business of Nantahala or of Nantahala's parent company, Aluminum Company of America and its subsidiaries in North Carolina, Tapoco, and Yadkin, Inc."

As the record of this proceeding prior to remand established—and as the Supreme Court found (299 N.C. at page 435):

> "The transmission facilities of Nantahala and Tapoco are integrated and interconnected into a single system. Alcoa controls the ultimate operation and accounting policies of both utilities. The chief executive officers of both Nantahala and Tapoco report directly to an Alcoa vice president. Members of the board of directors of both utilities are employees of Alcoa."

Alcoa's dominance is obviously and frequently documented in the results of various arrangements it has caused Nantahala and Tapoco to enter into. Such dominance has caused detriment to Nantahala and has resulted in the passing of concealed benefits to Alcoa.

Therefore, based upon the foregoing and upon careful consideration of the entire evidence of record, the Commission concludes that it should reject the companies' proposed allocation methodology in that said methodology in all material respects is based upon the New Fontana Agreement and the Tapoco-Nantahala Apportionment Agreement.

Before going forward with a specific discussion of the Intervenors' allocation methodology, it is appropriate to examine two questions which were vigorously contended as between Alcoa and Tapoco on the one hand and the Intervenors on the other hand:

First, does Tapoco wheel power for Alcoa?

The companies (Alcoa and Tapoco) contend that the $31 million of power purchased by Alcoa directly from TVA can become a part of the Nantahala-Tapoco system simply because the power was allegedly "wheeled" by Tapoco from TVA to Alcoa.

Alcoa purchases supplemental power from TVA. Alcoa and Tapoco contend that the TVA purchased power is wheeled to Alcoa through Tapoco's facilities. The Intervenors rigorously dispute this contention on the grounds that there is neither wheeling in fact, nor a contract between TVA and Tapoco, nor Alcoa and Tapoco, nor Alcoa and TVA for Tapoco to perform wheeling services, nor is there a charge made for wheeling services.

Company witness Buchanan, "an accounting executive with the title of Assistant Controller-Financial Accounting" for Alcoa (Vol. 2, Tr. p. 86), testified that:

> ". . . As Assistant Controller of Alcoa, I have general responsibility for the financial accounting for Alcoa and its subsidiaries, and as such have responsibility for the books and records and financial policies of Tapoco and Nantahala." (Vol. 2, Tr. p. 87)

On cross-examination he was asked:

"Q. Does Tapoco ever receive a fee for the wheeling service you have just described?

A. I'm not aware of any fee, no, sir." (Vol. 2, Tr. p. 143)

Immediately after that testimony, Company Counsel Jones argued:

"... that the record in this proceeding carries with testimony of the earlier witness, Mr. George Myers, President of Tapoco, a complete discription of the wheeling, recognition that the wheeling is pursuant to Tapoco's FERC rate schedule No. 4, I believe it is, although the record will speak for itself . . ." (Vol. 2, Tr. pp. 143-144)

However, reference to the prior testimony of Mr. Myers fails to bear out Counsel Jones' contention. Mr. Myers had testified:

"Q. Do you know whether Tapoco has an FERC rate schedule covering its wheeling of Alcoa's purchases from TVA to the other two plants?

A. I guess I'm not familiar with what that rate schedule is. I know the basis on which it is done but I don't know the exact rate schedule." (E-13, Sub 29, August 29, 1980, Vol. 1, Tr. pp. 65-66)

Switching back to accounting officer Buchanan, inquiry was made of him as to whether he could identify the alleged wheeling contract. On cross-examination Mr. Buchanan testified:

"Q. All right. Now, you are saying then I gather that Tapoco transmits TVA to Alcoa. Is that correct?

A. Yes, sir.

Q. All right. Now, will you tell the Commission, please, sir, on what agreement you rely for making that statement and have you seen that agreement?

A. I have not seen the agreement.

Q. You don't know it to be a fact, do you?

A. No, sir." (Vol. 2, Tr. p. 139)

Thus we observe that neither the President nor chief financial officer of Tapoco was familiar with the alleged wheeling contract. Moreover, if there is a wheeling contract, certainly it does not provide compensation to Tapoco for any wheeling service performed.

Wheeling has a particular definition. In *Town of Norwood* v. *FERC*, 587 F. 2d 1306 (1978), at page 1307, Note 2, the Court defined wheeling this way:

" . . . wheeling is an industry term which denotes the use of one utility's transmission facilities to transmit from another utility."

In *Idaho Power* v. *FPC* 346 F. 2d 956 (1965), at page 957, Note 1, the Court said:

" 'Wheeling' is the transmission of one company's power over another company's system."

And, see *Utah Power & Light Co.*, v. *Morton*, 504 F. 2d 728 (1974).

These definitions of "wheeling" are compatible with the definition of "wheeling" within the electrical industry. Thus, within the electrical industry "wheeling" is defined as follows:

"Wheeling service—the use of the transmission facilities of one system to transmit power of and for another system." (Intervenors' Judicial Notice Ex., Edison Electrical Institute, "Electric Utility Rate Making and Load Management Terms," dated Sept. 11, 1978, p. 83)

The companies (Alcoa and Tapoco) subsequently had their witnesses identify a contract between Alcoa and Tapoco as the one governing the alleged "wheeling" arrangement. Buchanan testimony, Vol. 3, Tr. pp. 1-2; Vander Veen testimony, Vol. 4, Tr. pp. 2, 11-14. However, that contract (Intervenors' Buchanan Cross Exam. Ex. 2) does not mention either "wheeling" or "trans-

mission" to support the companies' position. Instead, the witnesses must interpolate other words as including within their framework "wheeling." Such interpolation was accomplished by accounting witness Buchanan in this fashion:

"Q. I will hand you the document, sir, and ask you, please, to point out to me wherein in this document you find language that supports that characterization of it, please?

A. The contract reads to the effect under which power delivered to Alcoa, Tapoco and other sources, is transferred and switched at the high voltage substation facilities of Tapoco, located adjacent to the Alcoa, Tennessee, works of Alcoa. And it is my understanding that that relates to the wheeling between the various plant locations of the Alcoa, Tennessee, plant.

Q. That is your understanding. It doesn't say that, does it?

A. Not in those words, no, sir.

Q. It doesn't say that in any words, does it?

A. No, sir."
(Vol. 3, Tr. pp. 2-3)

Company Witness Vander Veen testified that transforming and switching constituted the alleged wheeling.

"Q. . . . I'm going to read to you, sir, the initial paragraph lower case 'a.' quote, 'At the substation facilities mentioned above, Tapoco will perform such necessary transformation and switching of power delivered to Alcoa as Alcoa shall direct.' End quote. I ask you first, sir, is there anything in that language that relates to transmission?

A. Yes, sir. Those functions, the switching functions, if I could see the word please. Yes, such necessary transformation and switching of power—

Q. (Interposing) Transformation?

A. Transformation and switching, those are transmission functions, sir." (Vol. 4, Tr. p. 5)

Later, the so-called wheeling was pin-pointed to a single location.

"Q. Does either pay the other any wheeling charge whatever for the transmission of that power from any generating source to the Tapoco substation?

A. The wheeling is at the substation.

Q. That's the only point?

A. Yes, sir."
(Vol. 4, Tr. p. 11)

The Agreement is not in actuality a wheeling agreement since "wheeling" requires transmission and the agreement is dealing with transformation and switching.

In actuality, there is no wheeling of power for Alcoa or TVA by Tapoco.

In further support of this position, the Commission takes note of the fact that Tapoco sells all of its power, i.e., its NFA return entitlement from TVA, to Alcoa. Intervenors' Buchanan Cross-Examination Ex. 3 is that 1963 sales arrangement.

The companies urge that the Alcoa purchases from TVA be considered in the Nantahala-Tapoco electrical system as the result of the following paragraph in the alleged wheeling contract from Tapoco to Alcoa.

"It is desirable to reduce to writing the arrangement between Tapoco, Inc. (Tapoco) and Aluminum Company of America (Alcoa) under which power delivered to Alcoa (from Tapoco and other sources) is transformed and switched at the high voltage substation facilities of Tapoco, located adjacent to the Alcoa, Tennessee works of Alcoa. Accordingly it is proposed that we agree as follows:

(Intervenors' Buchanan Cross-Examination Ex. 2)

For accounting purposes that contractual language obviously doesn't carry with it a wheeling obligation since no wheeling fee is collected. Even the president of the company isn't aware of a wheeling obligation by virtue of that contract. Even if the contract marginally constitutes a wheeling arrangement, it should not be used as a ploy to dump Alcoa's purchases from TVA into the Nantahala-Tapoco electrical system.

Perhaps the truth of the separateness of Alcoa's TVA purchases from the Nantahala-Tapoco system is best summed up by this honest and final testimony of the companies' witness Dr. Leininger when he testified:

> "Q. All right. Now you say each must employ additional TVA power to meet its customers' total load. When you make that statement, are you saying that Tapoco supplementally to the entitlements it gets out of the Fontana Agreement must acquire TVA power to supply to Alcoa?
>
> A. I suspect its inartful wording. Alcoa does its own purchasing as I understand it.
>
> Q. Did you understand that when you wrote this sentence?
>
> A. Yes, sir.
>
> Q. Why did you write it this way then?
>
> A. Because I wasn't careful when I wrote it."
> (Vol. 14, Tr. p. 97)

Therefore, based upon the foregoing and other evidence of record, the Commission concludes that it would be completely erroneous to find either (1) that the Alcoa purchases from TVA are "wheeled" by Tapoco to Alcoa or (2) that such power, if wheeled, enters into and becomes a part of the Nantahala-Tapoco unified public utility system.

The second question is: Are Alcoa's purchases of power from TVA part of the Nantahala-Tapoco integrated system?

The record reflects, during the year 1975, that Alcoa bought some $31 million in electric power from TVA which Alcoa used solely for its industrial plant operations in Tennessee. The record establishes without dispute that neither Nantahala nor Tapoco generated, bought, sold, acquired, or had any right to use that electricity. Alcoa retained 100% control over such power at all times. Where Nantahala and Tapoco, as public utilities, do not generate, acquire, buy, sell, or have the right to control the use of electric power, no such ungenerated, unacquired, unbought, unsold, and uncontrolled power can be a part of the Nantahala-Tapoco public utility system.

However, assuming *arguendo* the companies' contentions regarding wheeling are correct there is no showing that the power is at all integrated with the combined system. The further issue is whether the power purchased by Alcoa directly from TVA has become available to the Nantahala-Tapoco system to meet its public service load. If Tapoco had any contact at all with the Alcoa purchases from TVA, at most, the Tapoco activities are limited to Transforming and Switching, which activities do not rise to the level of transmission as required for wheeling. However, if it is assumed, again for purposes of argument, that Tapoco did "wheel" the Alcoa Power purchased from TVA, such power should not be treated as a part of the Nantahala-Tapoco unified system because the power never entered into the Nantahala-Tapoco unified system. Even if the TVA power enters Tapoco's substation at Alcoa, Tennessee, such power does not traverse the Nantahala-Tapoco electrical system. Instead, at most, that power is released by TVA at the Alcoa substation where it is transformed and immediately switched over to Alcoa's lines. Such power could never be made available to serve any portion of the public service load. Most fundamentally, its identity as Alcoa power is never lost since Alcoa never releases control of the use of that power in its capacity as ultimate consumer of that power from TVA.

The contract between Alcoa and TVA (Company Exhibit BDC-3) does not mention delivery of the TVA purchased power by the Nantahala-Tapoco system but rather describes delivery direct to Alcoa. Page 2, paragraph 3, of the contract reads as follows:

> "3. *Delivery of Power.* Power delivered hereunder shall be 3-phased alternating current at a frequency of approximately 60 cycles per second and shall be delivered at company's Alcoa Primary Substation at a normal voltage of 162 Kw or such other voltage as may be agreed upon by the operating representatives. Except for temporary periods of abnormal operating conditions, voltage variations will not exceed 5 percent up or down from the normal voltage."

Even when interpreting "Company's Alcoa Primary Substation" to mean a Tapoco substation, obviously Alcoa does not lose any control over that purchased power by permitting it to become a part of the Nantahala-Tapoco unified system.

Moreover, Alcoa does not pay a fee, even a nominal one, to Tapoco for the so-called "wheeling" service—if there is a "wheeling" service. This is made clear by the testimony of companies' witness Buchanan.

> "Q. Then Tapoco, the combined Nantahala-Tapoco system or entity, however you want to characterize it, neither billed nor received a penny with respect to TVA sales to Alcoa. Isn't that correct, sir?
>
> * * * * *
>
> "A. You are correct in the statement in the manner in which you said it. Yes, sir—." (Vol. 2, Tr. pp. 118-119) (See, Vol. 2, Tr. p. 134)

Additionally, Tapoco failed to report on its Form 1 to FERC that it wheeled $31 million of power to Alcoa (Vol. 2, Tr. p. 134). One reason for this "failure" is that TVA bills Alcoa directly for the power. Tapoco does not become involved with the purchased power, either financially or through line losses.

The Commission, based upon the foregoing and other evidence of record, concludes that purchases of power from TVA by Alcoa are not cost applicable to the Nantahala-Tapoco integrated system properly assignable in any way to said system's North Carolina retail operations.

Allocation of the costs of the Nantahala-Tapoco unified system involves several aspects, namely, (a) allocation of the $31 million of Alcoa purchases from TVA and (b) the mathematics of allocation. We will treat these two items separately.

A. *Allocation of the $31 Million of Alcoa Purchases From TVA*

The Intervenors contend and the Commission concurs that should the $31 million of Alcoa purchases from TVA be rolled into the Nantahala-Tapoco unified system, those purchases should be allocated entirely to Alcoa.

To illustrate the necessity of the allocation entirely to Alcoa, let us suppose that Tapoco purchased the power in question under a contract identical to the Alcoa-TVA contract. In such an instance there is no way in which that contract can be turned from a specific requirements contract into a general requirements contract. The Alcoa-TVA power purchase agreement (Applicant Exhibit BDC-3), at page 2 (discovery p. 200082), states:

> "2. *Availability of Power.* Subject to the other provisions of this contract, TVA shall make available to Company hereunder 'firm power' in the respective amounts specified for the periods indicated in the tabulation set forth below, which amounts shall be 'firm contract demand' under this contract for such periods.

	Amount of Firm Power Available
August 1, 1969, through December 31, 1972	30,000 Kw
January 1, 1973, through July 31, 1979.	350,000 Kw

> Except as otherwise provided in this contract, TVA will make power available to company continuously hereunder during each of the above periods in the amount of the firm contract demand specified for that period. The firm power available hereunder will be deemed to be taken and used by the Company at 100 percent load factor."

The terminology of the contract is not suitable for a public utility load, which needs variable amounts of energy, but rather is suitable only for a specific customer having stable needs. Thus, even if the contract were considered to be a Tapoco contract, the contract is so tailored to a specific customer that the costs associated with it would have to be specifically assigned to the customer. This logic is confirmed by the testimony of Intervenors' witness Springs wherein, on cross-examination by the companies, he testified:

> "Q. That power was purchased for that one customer, is that right?
>
> A. That is right. It would be a pass-through because it is identified as related to that customer. It is not a function of a utility." (Vol. 15, Tr. p. 81)

In this case, in order to escape a specific or pass-through assignment of costs of the TVA purchases to Alcoa, the contract would have to be modified to be a Tapoco purchase contract with modified terms providing for power amenable to a public utility operation. Neither of those facts has or will happen. For purposes of this case, the companies are bound to the existing contract to which Tapoco is not a party and which is an Alcoa specific requirement rather than a general requirements contract. As companies' witness Cockrell testified:

> ". . . Alcoa purchases Tapoco's entitlements and acquires the remainder of its needs from TVA under a companion contract." (Vol. 5, Tr. p. 62)

Alcoa is not a small industrial company which would have only a marginal effect on Nantahala but rather a massive company with worldwide operations. Gross revenues in 1980 were $5.2 billion (Vol. 2, Tr. p. 110), which amount is more than 300 times the gross revenues of Nantahala. The Alcoa, Tennessee, aluminum reduction facilities, as late as 1952, when the book *An American Enterprise* was written (Intervenors' Exhibit DAS-1, p. 1 of 14), was the largest in the world (Intervenors' Exhibit DAS-1, p. 8 of 14). Furthermore, the Alcoa, Tennessee, aluminum reduction plant is merely one of many for Alcoa. See Applicant's Exhibit BDC-1 for a list of Alcoa's nine aluminum production plants which have an annual average need of 28,557,600,000 Kwh of electricity (3260 Mw x 24 x 365). By way of comparison, Alcoa's annual aluminum production need for electricity approaches in size the combined North Carolina production of both Duke Power Company and Carolina Power & Light Company.

Alcoa is a gigantic energy consuming entity nationwide and its impact on western North Carolina is likewise enormous. If the Alcoa, Tennessee, load that is purchased from TVA were to be assigned as a function of the Nantahala-Tapoco system, the impact of that load on the system would be so enormous as to warp and twist the costing technique of the entire system. Indeed, if the Nantahala-Tapoco system tried independently to service the Alcoa-Tennessee load, it would have to double its system size. Yet no effort has been made by the system to do that. Neither Nantahala nor Tapoco has built a facility in over 20 years. Alcoa is entirely dependent upon TVA for its supplemental load.

B. *The Mathematics of Allocation*

Although the Commission has previously rejected the companies' use of demand and energy entitlements contained in the NFA and the Apportionment Agreement as a basis for the derivation of demand and energy allocations, the Commission

believes that the manner in which the companies employed the data contained in said agreements is worthy of further comment.

The NFA return entitlement from TVA is an annual average of 218,300 Kw of which Nantahala is assigned 41,300 Kw leaving the balance, less line losses, for Tapoco. While 90 Mw of the entitlement is curtailable for as long as five months annually, total energy curtailed is limited to 1,260,000,000 Kwh during the entire 20-year term of the agreement (Item 9, A.G. Popovich Cross-Examination 4, pp. 6-7). Of course, if power is curtailed in one year it will have to be made up in the other years in order for TVA to supply an annual average of 218,300 Kw over the 20-year term. Despite this, for allocation of demand costs to Tapoco when computing the system peak, Company witness Vander Veen did not include any portion of the 90 Mw curtailment entitlement for determining the peak demand upon the system. Witness Vander Veen testified:

> ". . . Consequently, for demand cost allocation purposes, I used only firm power available to meet system peak, thus removing the amount of capacity that can be curtailed and interrupted from the capacity available to serve system peak load. . . ." (Vol. 3, Tr. p. 71)

The upshot of this technique is to render the 90 Mw valueless for meeting the system demand at any time, even during years when there is no curtailment and, indeed, when there may be additional make-up demand.

Mr. Vander Veen also took out of the Tapoco demand allocation 1/6th (i.e. 15 Mw) of the 90 Mw interruptible power returned by TVA under the NFA. A total of 105 Mw was thus taken out of Tapoco's demand allocation for both the curtailable and the interruptible power (Vol. 3, Tr. p. 71).

The effect on Nantahala of Mr. Vander Veen's technique will be to dramatically increase Nantahala's proportionate share of the demand charges. A careful analysis of Mr. Vander Veen's

allocation calculation shows the following: His system peak is 430.2 Mw, as to which there is improperly included 235 Mw representing Alcoa's TVA purchases. If we deduct the 235 Mw from the system peak of 430.2 Mw, we obtain a Nantahala-Tapoco system peak of 192.20 Mw of which Mr. Vander Veen calculates Nantahala's share to be 107.2 Mw while Tapoco's share is only 88 Mw (Vol. 3, Tr. p. 772). Thus, Nantahala must share a considerably higher demand allocation than Tapoco even though Nantahala and Tapoco both take under the NFA and Tapoco takes three times as much power as Nantahala.

Witness Springs explained how Mr. Vander Veen's approach unfairly burdens the public customers by requiring them to bear costs properly assignable to Alcoa.

> "Mr. Vander Veen assigns customer cost by utilizing the entitlements of the New Fontana Agreement to derive the system demand instead of utilizing the total demands placed upon the Tapoco and NP&L generation. Although the New Fontana Agreement reshaped the available power supply to suit Alcoa's load requirements, the entitlements result from the investment, maintenance, and operation costs necessary to make the hydroelectric generation of NP&L and Tapoco available for TVA's demands.
>
> The fallacy of Mr. Vander Veen's approach is illustrated by the demand credit he assigns to Alcoa because of the interruption and curtailment features of the New Fontana Agreement entitlements. This is a misapplication of an allocation principle. Although it is not unusual for an industrial customer to receive a credit for accepting interruptible power, the rationale for this is that the utility providing the service to that customer will save the cost of carrying reserves. The ability of a utility to provide such credits is limited by its need for reserves. There should be no credit for interruptions which do not result in cost savings to the supplying utility. Mr. Vander Veen's demand credit unfairly assigns to other customers the fixed costs necessary to generate the power traded to TVA for this curtailable and interruptible power. The fixed costs of investment, operation, and

maintenance for these plants do not cease when TVA curtails delivery to Alcoa under the New Fontana Agreement contractural arrangements." (Vol. 15, Tr. pp. 59-60)

Mr. Vander Veen arrived at his allocations based upon the premise that the NFA and the 1971 Apportionment Agreement were negotiated in the best interest of Nantahala's public service load. Nothing could be further from the truth! (Vol. 15, Tr. p. 39)

The NFA was entered into for and structured to meet Alcoa's load requirements. Nantahala was not even present during negotiations (Intervenors' Exhibit DAS-25). In essence, the NFA is a trade-off of certain firm power and secondary power, available less than 50% of the time, for lesser amounts of firm and secondary power that are curtailable and interruptible but available more than 50% of the time, since any power available more than 50% of the time is useable by Alcoa in its aluminum smeltering operations (Vol. 15, Tr. p. 40). The trade-off result is a considerable improvement in the value of Tapoco's energy useable for Alcoa's aluminum production (Vol. 15, Tr. p. 45). The trade-off has no value to the public load. Alcoa (Tapoco) should, therefore, take full cost responsibility for the demand-related costs associated with the capacity traded off (Vol. 15, Tr. p. 61).

The Vander Veen demand allocation technique would result in a gross inequity to Nantahala and to public load customers. A proper allocation technique should not be inequitable either to Nantahala or to Tapoco.

With the terms of the NFA having been structured to meet Alcoa's industrial needs and not Nantahala's public service needs, it is improper to allocate demand and energy costs based upon the TVA return entitlements. Rather, demand and energy charges should be based upon the capabilities and the needs of Nantahala and Tapoco outside of the TVA return entitlements. That is the very purpose of the roll-in study.

The combination of the NFA and the 1971 Apportionment Agreement forces Nantahala to purchase additional power irre-

spective of its production capacity. We reiterate what the Supreme Court said in *Utilities Commission* v. *Edmisten, supra,* at page 440:

> ". . . Suffice it to say that the assertion that Nantahala's public is fairly served by a contract requiring Nantahala to purchase additional power regardless of the adequacy of its own generation assaults the common sense of this court. Nantahala's customers should not be denied the benefit of their utility's fairly regular harvests of abundant energy."

The Commission also points out again that the purpose of the roll-in method of ratemaking is to "cancel" or at least to "true-up," concealed benefits. See, *Utilities Commission* v. *Edmisten, supra,* at pages 437-443.

The Intervenors contend that the following data represents the capabilities and needs of the Nantahala-Tapoco unified system, and that such data is appropriate for use in the allocation of demand related costs.

A. Dependable Capacity for NP&L Projects (See Intervenors' Exhibit DAS-4)	85.4 Mw
B. Dependable Capacity of Tapoco Projects (See Intervenors' Exhibit DAS-4)	302.8 Mw
C. Total (A + B)	388.2 Mw
D. Less Reserve at 3%	11.3 Mw
E. Net *Firm* Capacity Available to Meet the Load (C-D)	376.9 Mw
F. Purchase Power of NP&L from TVA (NP&L FPC Form No. 1, 1975, page 422)	50.4 Mw
G. Losses on F above (assumed 5%)	2.5 Mw
H. Total Net *Firm* Capability Available at Generation to Meet the System Requirements of NP&L and Tapoco (E + F + G)	429.8 Mw

See Vol. 15, 54, p. 62.

Nantahala's peak load during the test year was 105,747 Kw which figure represents its maximum need during the year. Nantahala's demand responsibility for costing purposes can be calculated by dividing the total Nantahala-Tapoco system demand responsibility into Nantahala's maximum demand responsibility. Thus, dividing 429,800 Kw into 105,747 Kw produces a Nantahala demand allocation of 24.60% of the system's demand responsibility (Vol. 15, Tr. p. 634). Using this allocation factor, 24.60% of the Nantahala-Tapoco unified system demand costs should be assigned to Nantahala and the balance to Tapoco.

While demand charge allocations must be computed based on production capacity and capacity needs, energy charge allocations must be computed based upon the average energy available for the Nantahala-Tapoco unified system plus Nantahala's purchases. The Intervenors contend that the following data represent the average energy available to the combined system including Nantahala purchases, and that such data is appropriate for use in the allocation of energy related costs.

A.	Average Energy Available from NP&L Projects (New Fontana Agreement Apportionment Study) (Intervenors' Exhibit DAS-12)	391,500 Mwh
B.	Average Energy Available from Tapoco's Projects (New Fontana Agreement Apportionment Study) (Intervenors' Exhibit DAS-12)	1,373,600 Mwh
C.	Total Average Energy Available from NP&L and Tapoco's Projects (A + B)	1,765,100 Mwh
D.	NP&L Purchase of Energy from TVA (NP&L Form No. 1, page 422)	81,265 Mwh
E.	Losses on D above (assumed 5%)	4,063 Mwh
F.	Total Average Energy Available to Meet System Load (C + D + E)	1,850,428 Mwh

See, Vol. 15, Tr. pp. 63–64.

Nantahala's energy requirement during 1975 was 453,548 Mwh. Nantahala's energy responsibility for costing purposes can be calculated by dividing the total Nantahala-Tapoco system energy responsibility into Nantahala's energy responsibility. Thus, dividing 1,850,428 Mwh into 453,548 Mwh produces a Nantahala energy responsibility of 24.51% (Vol. 15, Tr. pp. 64–65). Using this allocation factor, 24.51% of the Nantahala-Tapoco unified energy costs should be assigned to Nantahala and the balance to Tapoco.

The demand allocation factor of 24.60% and the energy allocation factor of 24.51% were used by Intervenors' expert witness Solomon in allocating the Nantahala-Tapoco total system demand and energy related costs to said system's North Carolina retail operations.

The Commission, after having very carefully considered the entire evidence of record with respect to the assignment of cost including cost allocation techniques and/or methodologies, concludes that the methods and procedures employed by the Intervenors with respect hereto are, in all material respects, proper and that said methods and procedures should be adopted for use herein.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 7, 8, 9, 10, AND 11

There is no disagreement between the parties with respect to the reasonable original cost, the replacement cost, the depreciation reserves, or the allowance for working capital applicable to the total combined operations of the Nantahala-Tapoco system. There is, however, a difference of opinion as to the proper amounts of the aforementioned costs and reserves applicable to the combined system's North Carolina retail operations. This difference results from the application of different allocation methodologies which have been previously discussed and from the

Intervenors' contention that no fair value increment should be assigned to the property of Tapoco. As previously stated, the Commission has adopted the allocation methodology proposed by the Intervenors for use herein. Therefore, it is entirely consistent and proper for the Commission to adopt North Carolina retail levels of investment and depreciation reserve resulting from application of said Intervenors' allocation techniques. With respect to the Intervenors' contention that no fair value increment should be added to the original cost of Tapoco's property, the Commission is compelled by G.S. 62-133, as it was structured during the test year and at the time of the Commission's initial decision in this matter, to reject the Intervenor's position in this regard.

Therefore, based upon the foregoing and the entire evidence of record, the Commission concludes that the reasonable original cost less depreciation of the Nantahala-Tapoco property used and useful in providing electric service to its retail customers in North Carolina is $18,749,000 (original cost of $36,951,000 less depreciation reserve of $18,202,000); that the reasonable replacement cost of said property is $57,795,000; that the fair value of Nantahala-Tapoco's utility plant used and useful in providing electric service to its retail customers in North Carolina giving a 40% weighting to original cost less depreciation and a 60% weighting to the trended original cost less depreciation is $42,177,000; that said fair value includes a reasonable fair value increment of $23,428,000; that the reasonable allowance for working capital net of customer deposits is $925,000 ($1,113,000 - $188,000); and that the total reasonable fair value of Nantahala-Tapoco's property in service to its North Carolina retail customers is $43,102,000.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 12 AND 13

With respect to the test year level of operating revenue and operating revenue deductions the differences between the parties arise, in all material respects, as a result of the use of different

allocation techniques and as a result of Intervenor witness Solomon having excluded certain revenue and revenue-related expense adjustments of Company witness Vander Veen from the total combined Nantahala-Tapoco system operations.

The Commission has previously adopted the allocation techniques employed by the Intervenors for use herein. The revenue and revenue-related expense adjustments of witness Vander Veen excluded from witness Solomon's total system cost-of-service determination relate to non-Fontana agreement power purchased from TVA to serve the Alcoa load. As a result of the methodology employed in the assignment or allocation of costs proposed by Intervenor witnesses Springs and Solomon and that adopted by the Commission, neither inclusion or exclusion of said revenue and expense adjustments would have any effect upon the combined system's North Carolina operations.

The Commission, therefore, concludes, based upon the entire evidence of record, that the test year level of operating revenue of $11,067,00 and operating revenue deductions including taxes and interest on customer deposits of $8,322,000 are proper for use herein. Said levels of revenue and operating revenue deductions are those proposed by the Intervenors with one minor exception. The exception being that the level of income tax expense proposed by witness Solomon has been adjusted to reflect the impact of a slightly different level of interest expense assigned by the Commission to the Nantahala-Tapoco system's North Carolina retail operations (see Schedule II contained herein).

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 14, 15, 16, AND 17

The capital structure, the embedded cost of debt, and the proper equity and overall rates of return for Nantahala were established in the June 14, 1977, Commission Order entered in this

case. As much as possible, Tapoco and the Nantahala-Tapoco unified system should be similarly treated in this remanded hearing although certain adjustments are necessary.

Prior to the original filing in this case, Nantahala had been permitted, in Docket No. E-13, Sub 26, to restate depreciation of its assets from accelerated depreciation actually taken to normal straight-line depreciation. At that time the Commission ordered that approximately 48% of the restated depreciation be treated as deferred income taxes. The remaining balance of approximately 52% was credited to capital as retained earnings.

In the current case, Tapoco seeks to restate its accelerated depreciation to normal straight-line depreciation as was allowed for Nantahala in Docket No. E-13, Sub 26. This difference between the accelerated and straight-line depreciation technique is $15,705,393. The Intervenors do not object to the restatement of depreciation provided it is handled similarly to Nantahala's. Accordingly, the Intervenors contend that 48% of the $15,705,393, which is $7,538,589, should be credited to deferred income taxes and treated as cost-free capital (Solomon prefiled testimony, p. 7).

The Companies contend, if they are required to reflect restatement of the depreciation reserve account in the manner proposed by the Intervenors, that said restatement will result in an overrecovery of costs from Alcoa. Further, the Companies argue that such credit has been made (Vol. 20, tr. p. 19). Intervenors vigorously disagree with this assertion. Reference to Companies' Ex. RDB-R4, pp. 4-5 of 5, shows that the only cost-free capital which they have proposed for the combined Companies is $4,753,925 which is identified as Nantahala's cost-free capital (See Intervenor's Ex. JBS-1, p. 1 of 3).

The Commission, after having very carefully considered the entire evidence of record with respect hereto, concludes that the level of deferred income taxes proposed by the Intervenors of approximately $12,292,000 is proper for use herein.

With respect to the proper level of debt and equity capitalization for Tapoco, the Intervenors contend that such capitalization should be based upon the industry norm. More specifically, the Intervenors contend that the average capital component ratios of a group of 100 electric utilities actually maintained during the period 1975-1979, as compiled by the First Boston Corporation, are proper for use herein. The Companies disagree with the Intervenors, contending that the utilities included in the First Boston survey are in no way financially analogous to Tapoco. The Commission agrees with the Companies.

The Commission, therefore, concludes that the reasonable original cost capital structure for use herein is as follows:

Item	Percent
Debt	40.05
Common equity	37.00
Cost-free	22.95
Total	100.00

and when the fair value increment is added, the reasonable fair value capital structure becomes:

Item	Percent
Debt	18.28
Common equity	71.24
Cost-free	10.48
Total	100.00

As previously stated, the Commission in its Order of June 14, 1977, found and concluded, for reasons stated therein, that a return of 4.20% on the fair value of Nantahala's investment in service to its North Carolina retail customers was just and reasonable and that rates should be set so as to allow the Company a reasonable opportunity to earn said rate of return. The Commission hereby reaffirms its finding and conclusion with respect thereto.

In passing, the Commission observes that, as a result of its actions herein, the rate of return the Company has been afforded an opportunity to earn on its original cost equity is far greater than that approved in the Commission Order of July 14, 1977.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 17, 18 AND 19

Based upon the findings of fact set forth herein above, the Commission concludes that the approximate annual level of revenues which Nantahala should be authorized to collect through rates charged for its sales of service is $9,032,000; that the rates and charges of Nantahala, based upon the adjusted test year level of operations, under rates approved by Commission Order of June 14, 1977, are excessive to the extent that said rates produce a level of revenue which is $2,035,000 ($11,067,000—$9,032,000) greater than the Applicant's revenue requirement (cost of service); that Nantahala should be required to reduce said rates and charges in a manner so as to achieve an annual gross revenue reduction of approximately $2,035,000, based upon the adjusted test year level of operations; and, that Nantahala should be required to refund to its North Carolina retail customers all revenue collected under the rates approved by Commission Order issued June 14, 1977, to the extent that said rates produced revenue in excess of the rates approved herein. Said refund shall include revenues collected under the Company's base rate structure as well as through operation of the Purchased Power Adjustment Clause plus interest computed and compounded at the legal annual rate. The methodology to be used in the determination of the level of excess revenues collected under the Purchased Power Adjustment Clause will be discussed subsequently.

The following charts summarize the gross revenues and the rates of return which the Company should have a reasonable opportunity to achieve, based upon the level of revenues approved herein. Such charts, illustrating the Company's gross revenue requirements, incorporate the findings, adjustments, and conclusions herein made by the Commission.

SCHEDULE I

NANTAHALA-TAPOCO COMBINED SYSTEM NORTH CAROLINA RETAIL OPERATIONS STATEMENT OF OPERATING INCOME, RATE BASE AND RATE OF RETURN TWELVE MONTHS ENDED DECEMBER 31, 1975 (000'S OMITTED)

Operating Income

Line No.	Item (a)	Present Rates (b)	Decrease Required (c)	Approved Rates (d)
1.	OPERATING REVENUES	$11,067	$2,035	$9,032
2.	OPERATING REVENUE DEDUCTIONS:			
3.	Purchased power	423	—	423
4.	Operation and maintenance	3,612	—	3,612
5.	Depreciation and amortization	1,133	—	1,133
6.	Taxes—other than income	1,004	122	882
7.	Taxes—Federal and State income	2,142	978	1,164
8.	Interest on customer deposits	8	—	8
9.	Total deductions	8,322	1,100	7,222
10.	OPERATING INCOME FOR RETURN	$ 2,745	$ 935	$1,810

Rate Base and Rate of Return

Line No.	Item (a)	Amount (b)
1.	ORIGINAL COST NET INVESTMENT:	
2.	Electric plant in service	$36,951
3.	Less: Accumulated depreciation	18,202
4.	Net plant in service	18,749
5.	Plus: Allowance for working capital	1,113
6.	Less: Customer deposits	188
7.	TOTAL ORIGINAL COST NET INVESTMENT	$19,674
8.	FAIR VALUE RATE BASE	$43,102
9.	FAIR VALUE RATE OF RETURN:	
10.	—Present rates	6.37%
11.	—Approved rates	4.20%

SCHEDULE II

NANTAHALA-TAPOCO COMBINED SYSTEM
NORTH CAROLINA RETAIL OPERATIONS
STATEMENT OF RETURN UNDER PRESENT AND APPROVED RATES
TWELVE MONTHS ENDED DECEMBER 31, 1975
(000's OMITTED)

PRESENT RATES
FAIR VALUE RATE BASE

Line No.	Capitalization (a)	Fair Value Rate Base (b)	Ratio (%) (c)	Cost Rate (%) (d)	Weighted Rate (%) (e)	Operating Income (f)
1.	Debt	$ 7,880	18.28	7.56	1.38	$ 596
2.	Equity[1]	30,707	71.24	7.00	4.99	2,149
3.	Cost-free	4,515	10.48	—	—	—
4.	Total	$43,102	100.00	—	6.37	2.745

APPROVED RATES
FAIR VALUE RATE BASE

Line No.	Capitalization (a)	Fair Value Rate Base (b)	Ratio (%) (c)	Cost Rate (%) (d)	Weighted Rate (%) (e)	Operating Income (f)
1.	Debt	$ 7,880	18.28	7.56	1.38	$ 596
2.	Equity[1]	30,707	71.24	3.95	2.82	1,214
3.	Cost-free	4,515	10.48	—	—	—
4.	Total	$43,102	100.00	—	4.20	1.810

[1]Original cost equity	$ 7,279
Fair value increment	23,428
Fair value equity	$30,707

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 20

The Commission has previously concluded that the reasonable test year level of operating revenue deductions applicable to the Applicant's North Carolina retail operations should include purchased power costs in the amount of $423,000.

Stated alternatively, the Commission has concluded that approximately 24.60% of Nantahala's total demand related purchased power cost and approximately 24.51% of Nantahala's total energy related purchased power cost is properly assignable to its North Carolina retail operations. Further, it is observed that the Commission in its decision on remand has included in the Applicant's North Carolina retail operations only 24.56% ($423,000/$1,722,000) of the cost of purchased power that was initially included by the Commission in its Order of June 14, 1977. Nantahala's Purchased Power Adjustment Clause allows the Company to recover virtually all of any increase in the cost of purchased power incurred over and above that included in its base rates. The Company under rates approved by Commission Order of June 14, 1977, has recovered, in all material respects, 100% of the increased cost of purchased power related to the level of purchased power included in the Company base rates. As previously stated, the Commission has now determined that only 24.56% or $423,000 of the purchased power cost of $1,722,000 initially included in the Applicant's cost of service is properly includable therein. Therefore, in the interest of fairness and equity, the Commission is compelled to find and conclude that to the extent the Applicant has recovered from its North Carolina retail customers via its Purchased Power Adjustment Clause increases in the cost of purchased power exceeding 24.60% of total Company (Nantahala) demand related increases and 24.51% of total Company (Nantahala) energy related increases, said recoveries are unjust and unreasonable and should be refunded to the Applicants' North Carolina retail customers. Further, the Commission con-

cludes that the purchased power base unit cost and the Purchased Power Adjustment Clause as they presently exist must be modified so as to conform with the Commission decision with respect thereto. More specifically, such clause should be formulated in a manner so as to permit recovery of only that portion of the increased cost of purchased power attributable to the Applicant's North Carolina retail operations, i.e., 24.56% of total Company demand related increases and 24.51% of total Company energy related increases.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 21

In its decision the Supreme Court stated as follows:

> ". . . we believe that essential fairness to all the parties is best served by allowing the increased rates to remain in effect, conditioned upon Nantahala's guarantee that it will in the future refund to its customers any overcharges should the new rates ultimately be determined excessive. Accordingly, we reverse the Court of Appeals' setting aside of the order of 14 June 1977 and direct the Commission to obtain adequate assurances of Nantahala's willingness and continued ability to refund such overcharges as may ultimately result from imposition of the 1977 rate schedule." 299 N.C., at 444.

In its Order of July 29, 1980, the Commission found and concluded that the rates approved for Nantahala in the Order of June 14, 1977, should be allowed to remain in effect pending further proceedings in this docket on condition that Nantahala file with the Commission an Undertaking to Refund, in a manner prescribed by the Commission, the amount, if any, found to be owing to its customers should the rates approved by the Order of June 14, 1977, be ultimately determined to be excessive after hearing on the remand from the Supreme Court.

On September 22, 1980, an Undertaking to Refund was filed by Nantahala.

On March 11, 1981, the Intervenors filed Motion to Require Alcoa and Tapoco to Join in the Execution of Nantahala's Undertaking to Refund or to Guarantee Nantahala's Continuing Financial Viability. In its Motion the Intervenors alleged that "[a]s a result of the operation by Alcoa of Nantahala and Tapoco as a single electric system, Nantahala has been and continues to be injured with 'concealed benefits' flowing from it to Alcoa and Tapoco." The Motion further alleged:

> "7. While the Nantahala ratepayers will be benefitted by the roll-in of Tapoco in rate making, the roll-in will not stop the flow of concealed benefits from Nantahala to Alcoa and Tapoco. This situation will be greatly exacerbated if, as Nantahala has several times predicted, rate refunds and lower rates resulting from a determination by this Commission favorable to intervenors would threaten Nantahala with bankruptcy. Alcoa should not be permitted to allow or cause Nantahala to go bankrupt when Alcoa itself is a party public utility in this proceeding and, through piercing of the corporate veil, responsible to the consuming public as such. Accordingly, Alcoa and Tapoco should be made to share in the "Undertaking To Refund," should a refund be ordered, for the protection of the financial soundness of Nantahala, or, in the alternative, should be required to guarantee Nantahala's ability to refund without injuring its viability as a public utility serving a public load in North Carolina."

On March 23, 1981, Alcoa and Tapoco filed its Response to the Intervenors' Motion. In their Motion Alcoa and Tapoco argued that the Intervenors' Motion was procedurally defective in that the relief sought was beyond the scope of the Supreme Court's remand, was in the nature of an untimely petition for reconsideration of the Commission's decision regarding Nantahala's undertaking, and was in the nature of a complaint and therefore beyond the scope of this proceeding. Alcoa and Tapoco also alleged that the relief sought by the Intervenors was beyond the Commission's jurisdiction over public utilities. Alcoa and Tapoco asked that the Intervenors' Motion be denied.

In this Order the Commision has found that Alcoa and Tapoco are public utilities; that Nantahala and Tapoco are wholly owned subsidiaries of Alcoa; that the Nantahala and Tapoco electric facilities constitute a single, integrated electric system and are operated by TVA as a coordinated part of the TVA system. The Commission has further found that for purposes of setting rates in this proceeding the Nantahala and Tapoco systems should be treated as one entity. Further, the Commission has found that the New Fontana Agreement, executed by TVA, Alcoa, Nantahala, and Tapoco, and the resultant 1971 Apportionment Agreement between Tapoco and Nantahala, have resulted in substantial benefits to Alcoa and significant detriment to the customers of Nantahala. Finally, the Commission has found that Alcoa has so dominated certain transactions and agreements affecting its wholly owned subsidiary Nantahala that Nantahala has been left but an empty shell, unable to act in its own self interest, let alone in the interest of its public utility customers in North Carolina.

The evidence in this proceeding discloses the inequities to Nantahala that arise out of both the New Fontana Agreement (NFA) and the 1971 Tapoco-Nantahala Apportionment Agreement. This evidence is fully described in Evidence and Conclusions for Findings of Fact Nos. 6 and 7. The detriment to Nantahala arising out of the 1971 Apportionment Agreement is summarized on page 19.

Moreover, the evidence in this proceeding, as fully described in Evidence and Conclusions for Findings of Fact Nos. 6 and 7, clearly and unambiguously demonstrates that the NFA was tailored to meet Alcoa's aluminum production needs with minimal consideration of Nantahala's public service needs in Western North Carolina. The Commission has noted elsewhere that Nantahala, while obligated under the original Fontana Agreement, was not a signatory thereto. The original Fontana Agreement still conveys significant benefits to Alcoa. Although Nantahala was a signatory to the New Fontana Agreement, it did

not participate in the negotiations of that agreement. Alcoa's dominance over its wholly owned subsidiaries Nantahala and Tapoco during the course of the New Fontana negotiations has resulted in substantial benefits to Alcoa and significant detriment to the customers of Nantahala. Tapoco is the conduit through which these benefits to Alcoa have flowed. Mr. Springs testified:

> "The 1963 Apportionment Contract shows on its face that the New Fontana Agreement was never intended as a 20-year power supply for NP&L public load. It appears that NP&L's officers and consultants were primarily concerned with the effect of the Agreement on the ongoing rate case and transfer cases before the NCUC and not with the interest of NP&L ratepayers over the 20-year period of Agreement."

The Commission must conclude that Alcoa has so dominated these transactions and agreements affecting its wholly owned subsidiary Nantahala that Nantahala has been left but an empty shell, unable to act in its own self interest, let alone in the interest of its public utility customers in North Carolina. Alcoa's domination of Nantahala in these transactions has resulted in Nantahala's collecting, through its base rates, excess revenue from its customers in the amount of approximately $2,035,000 a year since June 14, 1977. Moreover, this inequity is further magnified by the fact that Nantahala has collected significantly additional excess revenues through operation of its Purchased Power Adjustment Clause. Therefore, this Commission is compelled to order that, to the extent Nantahala is financially unable to make the revenue refunds required by this Order, Alcoa shall refund all or any portion of the aforementioned revenue refunds that Nantahala is financially unable to make.

IT IS, THEREFORE, ORDERED as follows:

1. That the approximate annual level of revenues which Nantahala is hereby authorized to collect through rates charged for its sales of service, based upon the adjusted test year level of operations, is $9,032,000.

2. That the rates and charges of Nantahala, based upon the adjusted test year level of operations, under rates approved by Commission Order of June 14, 1977, are excessive to the extent that said rates produce a level of revenue which is $2,035,000 ($11,067,000—$9,032,000) greater than the Applicant's revenue requirement (cost of service). Thus, Nantahala is hereby ordered to reduce said rates and charges by a uniform percentage across all rate schedules and charges in a manner so as to achieve an annual gross revenue reduction of approximately $2,035,000, based upon the adjusted test year level of operations.

3. That Nantahala is hereby ordered to refund to its North Carolina retail customers all revenue collected under the rates approved by Commission Order issued June 14, 1977, to the extent that said rates produced revenue in excess of the level of rates approved herein. Said refund shall include excess revenues collected under the Company's base rate structure as well as through operation of the Purchased Power Adjustment Clause calculated in a manner consistent with the findings and conclusions set forth herein plus interest computed and compounded at the legal annual rate.

4. That Nantahala shall file for Commission approval within 10 working days of the issuance date of this Order rates designed in accordance with the foregoing Ordering Paragraphs. Such rates shall include a Purchased Power Adjustment Clause formulated in a manner consistent with the Commission's findings and conclusions as set forth under Evidence and Conclusions for finding of Fact No. 20.

5. That Nantahala shall file for Commission approval within 30 days from the issuance date of this Order its plan for making the refunds as required herein. Further, Nantahala, at such time, shall file 10 copies of its calculation of the total amount of refund due including 10 copies of all detailed work papers associated therewith.

6. That, to the extent Nantahala is financially unable to make the revenue refunds required under Ordering Paragraph No. 3 above, Alcoa shall refund all or any portion of the aforementioned revenue refunds that Nantahala is financially unable to make.

7. That, except to the extent the Commission Order of June 14, 1977, is inconsistent with the findings and conclusions as set forth herein, said Order is hereby reaffirmed.

ISSUED BY ORDER OF THE COMMISSION.

This the 2nd day of September 1981.

NORTH CAROLINA
UTILITIES COMMISSION

Sandra J. Webster, Chief Clerk

(SEAL)

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APPENDIX D

Opinion Of The North Carolina Utilities Commission, dated January 28, 1982

State of North Carolina
Utilities Commission
,Raleigh

DOCKET NO. E-13, SUB 29

BEFORE THE
NORTH CAROLINA UTILITIES COMMISSION

In the Matter of

Application of Nantahala Power and Light Company for Authority to Adjust and Increase Its Electric Rates and Charges	FINAL ORDER OVERRULING EXCEPTIONS AND GIVING SUPPLEMENTARY CONCLUSIONS

BY THE COMMISSION: On September 2, 1981, a three member panel of the Commission issued an order in this docket which reduced rates and required refunds.

On October 19, 1981, Nantahala Power and Light Company (Nantahala) filed its Exceptions to and Notice of Appeal from the Panel's Order. Nantahala also filed Motion to Rescind, Alter or Amend Order and for Oral Argument and Further Hearings on Exceptions, and a brief in support of its exceptions.

On October 19, 1981, the Aluminum Company of America ("Alcoa") and Tapoco, Inc. ("Tapoco"), Respondents herein, also filed joint Exceptions to and Notice of Appeal from the Order of September 2, 1981. Alcoa and Tapoco also moved for reconsideration of the Panel's Order in light of their Exceptions and requested an opportunity to present oral argument on their exceptions before the full Commission. Tapoco and Alcoa also filed a brief ir support of their Exceptions.

On October 26, 1981, the Intervenors filed their Initial Response to the Applicant and the Respondents' several exceptions, notices of appeal, motions, and briefs and asked that they be denied, and in the alternative prayed that if the matters should be set for further consideration by the full Commission, that they be permitted an additional 30 days to file an additional response.

By Order issued on October 28, 1981, the exceptions of Applicant and the Respondents were scheduled for oral argument before the full Commission pursuant to G.S. 62-90(c) on December 7, 1981, and the Intervenors were permitted to file an additional response. On November 30, 1981, the Intervenors filed their joint Brief in Opposition to Exceptions.

On December 7, 1981, oral argument was held before the full Commission on the Exceptions of the Applicant and the Respondents. All parties were present and represented by counsel. On December 7, 1981, the Respondents, Alcoa and Tapoco, filed a Reply Brief to the Intervenors' Joint Brief, and during oral argument requested that this brief be accepted for consideration by the Commission. During the course of the oral argument, the parties addressed questions of federal law raised for the first time in this proceeding in the Respondents' Exceptions and Briefs filed in conjunction with their Notice of Appeal. During the argument, the Intervenors requested permission to further address these federal questions in writing after the oral argument. The Commission took under advisement the request to accept the Reply Brief and the request for permission to address the federal questions.

Subsequently, on December 16, 1981, the Commission entered an Order which accepted for consideration the Reply Brief and permitted all parties to file within 30 days "comments or memoranda or proposed findings with respect to the federal questions raised by the Respondents in their Brief and Exceptions to the Order of September 2, 1981." Nantahala and the Respondents have also filed Exceptions to this Order.

On January 15, 1982, the Intervenors filed with the Commission a proposed order styled "Intervenors' Proposed Order Entitled: Final Order Overruling Exceptions and Giving Supplemental Conclusions." On January 15, 1982, the Applicant, Nantahala, also filed its Response addressed to the federal questions. The Respondents, Alcoa and Tapoco, did not file. Respondents did, however, file on January 20, 1981, a Motion requesting the Commission to either reject the Intervenors' Proposed Order for the reason that it addressed issues other than federal questions, or in the alternative, to allow the Respondents an extension of time to file a counter proposed order.

Based upon a careful consideration of all the foregoing, the Commission concludes as follows:

I. The Intervenors' Proposed Order should be and has been accepted for consideration only insofar as it addresses "the federal questions raised by the Respondents." The Commission has accepted for consideration only the following portions of the Proposed Order:

- *Page 3*, Paragraphs III and IV

  Page 4, Paragraphs V and VII

  Page 4, The last Paragraph as it continues through line 16 on Page 5

  Page 7, Line 16 and continuing through Page 13, line 15

  Page 14, Paragraph B

The remaining portions of the Intervenors' Proposed Order are unresponsive in that they present arguments of other issues and have not been considered by the Commission. The Commission concludes that since it has not considered portions of Intervenors' Proposed Order which expands beyond the federal questions, the Applicants are not entitled to file a further proposed order which would encompass non-federal questions. Respondents have

previously chosen not to address the federal questions within the 30 days allowed except to the extent they have attempted to reserve them.

II. The Commission has carefully reconsidered each of the 21 separate Findings of Fact and the Evidence and Conclusions as to each Finding in the Panel's Order of September 2, 1981, in light of the Applicant's and the Respondents' exceptions thereto. The Commission concludes that each of the findings is fully supported by the evidence of record in this proceeding, and the Panel's conclusions of law are well reasoned and supported by the findings and the evidence. The Commission concludes that the Panel's Order should be affirmed.

In addition to the foregoing conclusions, the Commission makes the following supplemental conclusions relating to the federal questions raised by Respondents' Exceptions and Briefs:

III. The Applicant and Respondents may not reserve so-called "federal questions" for decision by another forum.

Both the Applicant and the Respondents attempted to expressly reserve certain so-called "federal questions" for submission to a federal tribunal. The Commission hereby rejects such attempts.

We observe that each of these "federal questions" inherently arose from the nature of the remand by the North Carolina Supreme Court, from the pleadings of all parties and from the total record of evidence placed before the Panel in this proceeding. Under these circumstances, the Commission does not believe that the doctrine of abstention as enunciated in the cases of *England* v. *Louisiana State Board*, 375 U.S. 411, 84 S. Ct. 461, 11 h. Ed. 2d 440 (1964) and *Government & Civic Employees* v. *Windsor*, 353 U.S. 364, 77S. Ct. 838, 1 L. Ed 2d 894 (1957) is either available or applicable to the so-called "federal questions" argued before us by Applicant and Respondents. In addition, the doctrine appears

to be available only when there is a prior or superior action pending in the federal court, which action is held in abeyance pending the disposition of certain non-federal questions in the state courts. Those circumstances do not exist here. This action has been proceeding in the state tribunals since 1975 (on remand since 1980) without the existence of any prior or superior federal cause of action.

In addition, given the great length of time over which this proceeding has already been contested, we firmly believe that it is incumbent upon this Commission to decide all questions over which this Commission has jurisdiction and to defer to others only questions over which this Commission has no jurisdiction. We conclude that the Commission has ample jurisdiction to hear and decide all issues raised in the remand, the pleadings, the evidence presented and the exception to the September 2, 1981 Order. Such questions have been heretofore or are herein decided.

IV. The Panel's Order is not precluded by exclusive federal regulation of interstate hydro power licensing, generation, sales and exchange operations; federal regulation of headwater benefits; or powers awarded to TVA by federal law.

A. *Part II of the Federal Power Act.*

1. The roll-in does not conflict with the preemptive jurisdiction of FERC to fix and regulate interstate wholesale electric rates.

The current docket is involved exclusively with the setting of retail rates for Nantahala. The case *does not involve* any attempt by this Commission to fix, establish, amend, alter, invalidate or modify rates or agreements approved by FERC. Not a single word of any of the contracts, apportionments or agreements as between TVA-Nantahala, TVA-Tapoco, Nantahala-Tapoco or Tapoco-Alcoa has been changed nor were any of the rates set by those agreements changed.

Indeed, the only thing which this Commission has done is to set retail rates for Nantahala pursuant to the remand of the North Carolina Supreme Court in the *Edmisten* case, 299 N.C. 432, 263 S.E. 2d 583 (1980). Having determined that the use of an appropriately performed roll-in of Nantahala and Tapoco (which is a question of *Fact*) would be beneficial to Nantahala's customers, the Panel concluded that rates based upon such roll-in should be placed into effect. With this conclusion the full Commission concurs.

It is entirely appropriate for a state commission to regulate retail rates. Congress has clearly indicated a desire to draw a bright line between federal regulation of interstate or wholesale rates and state regulation of intrastate or retail rates. *FPC* v. *So. California Edison,* 376 U.S. 205, 84 S. Ct. 644, 11 L.Ed 2d 638 (1944).

We conclude that the use of the roll-in as contained in the September 2 Order was in all respects proper, was consistent with the remand of the North Carolina Supreme Court and was not in conflict with FERC's jurisdiction over the various wholesale contracts, agreements and rates, either in law or in fact.

2. The September 2 Order does not intrude upon the authority vested in FERC by Part II of the Federal Power Act by failing to accept the costs of filed rates.

Several of the Agreements and contracts as between and among Nantahala, Tapoco, Alcoa and TVA constitute "filed rates" with FERC. What Applicant and Respondents apparently fail to realize is that no reasonable cost incurred by either Nantahala or Tapoco has been omitted from consideration. Every reasonable and proper cost was included in the data utilized and relied upon by the Panel in calculating the combined Nantahala-Tapoco cost of service on a roll-in basis.

The reason rates were lowered was not from a failure by the Panel to recognize legitimate costs, but because, as we have noted, the roll-in technique combines the lower cost of Tapoco production with the higher cost of Nantahala production. Since Nantahala and its customers are responsible for only about 24% of the combined Nantahala-Tapoco costs, Nantahala benefits from the roll-in and its rates can be lowered.

The costs of the Alcoa-TVA Supplemental Purchase Power Agreement were not included since these do not constitute a filed rate applicable to the Nantahala-Tapoco combined system. They are a separate matter entirely between TVA and one of its large industrial customers. Even if such costs had been included, they could properly have been attributed only to Alcoa and hence could not change the Commission's determination of the proper rates and charges for Nantahala.

3. The Panel's Order did not intrude upon the federal domain by disrupting the fabric of rates charged to Alcoa and Tapoco and TVA.

As noted, the September 2 Order does not infringe in any way upon the TVA-Alcoa Supplemental Purchase Power Agreement. Neither did such Order attempt, much less accomplish, any change whatsoever in rates charged by Tapoco to Alcoa. The Fontana Agreements, Apportionment Agreement and Alcoa Supplemental Power Agreement remain in effect exactly as before.

Again, at the risk of repetition, the roll-in is not a technique for disrupting the fabric of fixed economical relationships under filed FERC rates. It is, instead, merely a court approved method of combining financial data and allocating costs of the two companies, Nantahala and Tapoco, which have been found to constitute a single, integrated public utility system.

B. *Part I of the Federal Power Act*

The Commission does not agree with Applicant and Respondents that, by federal license, all of the hydroelectric production

from (or the economic benefit of) the four Tapoco dams are reserved exclusively for Alcoa. If the production were reserved exclusively for Alcoa, there could be no New Fontana Agreement (by which TVA exclusively generates and dispatches the power output of these dams). This output does not currently flow exclusively to Alcoa.

When Tapoco acquired ownership of two of these dams, Cheoah and Santeetlah, they were encumbered with an obligation to serve the public in North Carolina. In conjunction with the transfer, Tapoco was issued a certificate of public convenience and necessity in North Carolina, which imposes all the duties and responsibilities, including the duty to serve the public, of a public utility on Tapoco. Federal law requires, before a hydro license is issued, that the applicant submit evidence of compliance with state law concerning the operation of a public utility enterprise. The issuance of a federal license to construct and operate a hydroelectric project is a far cry from an edict by the federal licensing agency providing for the permanent allocation of the entire electrical energy output (or economic benefit) from the project. To the extent that the federal licenses for Tapoco's dams speak toward dedication of the electric energy, such dedication would of necessity include the using and consuming public of North Carolina.

In any event, the roll-in itself does not address the proposition (as we have earlier noted) of diverting Tapoco's actual energy production to the North Carolina public load. All the roll-in has accomplished is to allocate the costs of production of the Nantahala-Tapoco combined system, as between the North Carolina retail public load and the Alcoa manufacturing load. This allocation is no different from other allocations routinely performed by the Commission (e.g. for Duke, CP&L or Vepco) to distinguish between the North Carolina retail load and other loads over which the Commission has no jurisdiction.

C. *Regulation of Headwater Benefits.*

Again the Applicant and Respondents appear to believe, erroneously, that the Commission's September 2 Order in some way confers upstream benefits to Nantahala which are precluded by federal law and regulation. To the contrary, the so-called upstream benefits are a part of the Panel's overall discussion of concealed benefits accruing to Alcoa from the Fontana Agreement, New Fontana Agreement and the 1971 Apportionment Agreement. The sole reason for the entire discussion was not to provide a finite recovery to Nantahala of upstream benefits, but instead was required (a) to establish a foundation for the Panel's use of the roll-in methodology recommended by Intervenors as opposed to that recommended by the Applicant and Respondents, and (b) to show Alcoa's dominance over Nantahala and Tapoco which resulted in concealed benefits accruing to Alcoa.

D. *The Commission's September 2 Order does not interfere with the proper exercise of federal oversight by TVA.*

We reject the argument that the Panel's Order in any way contravenes the power of TVA to insure that the resale of power sold by TVA is reasonable and fair. The Commission's Order in no way challenges any rates set by or arguments entered into by TVA.

The authority of TVA cannot rationally be construed so as to extend to TVA the power to usurp proper rate setting authority now being exercised by FERC or by state commission. There is no evidence that TVA has ever done anything but accept retail/wholesale rates charged by its vendees, particularly when such rates were *fixed* and *established* by FERC or by a state commission.

We believe that unless and until this Commission enters an Order, which has not been done here, which injures or interferes with TVA's rates or operations, TVA not only will but must

accept such regulation of North Carolina retail rates by this Commission.

V. The Panel's September 2 Order does not impose unreasonable burden on interstate commerce.

The Commission does not view that the commerce clause of the United States Constitution has any more relevance to this proceeding than to a Duke, CP&L or Vepco retail rate proceeding. We repeat that the roll-in, as employed by the Panel, does no more than establish the overall cost of operation of the single, unified Nantahala-Tapoco system and allocate the proper portion of those costs to North Carolina retail customers for the purpose of fixing just and reasonable rates for Nantahala.

Even if it be assumed, *arguenda,* that the commerce clause is applicable to the current case, we do not believe that there has been any violation. The rule is that, where a local statute regulates evenhandedly to effectuate a legitimate local interest, and its effects on interstate commerce are only incidental, the local statute will be upheld unless the burden on interstate commerce is clearly excessive in relation to the local benefit.

The setting of retail electric rates for Nantahala's customers is clearly a legitimate North Carolina interest with a significant impact in this State. Since not a word of the contracts or agreements properly within the federal sphere has been changed, we do not believe that there is any impact on interstate commerce. Even if there is, such impact is clearly *de minimis* when compared to the local interest.

The public utility system organized, controlled and manipulated for so many years by Alcoa to serve its own manufacturing interests has now developed to such a degree that the local North Carolina interest demands that a proper allocation methodology be used so as to fairly distribute service costs between the North

Carolina retail ratepayers and Alcoa's manfacturing load. The roll-in technique adopted by the Panel accomplishes this goal without undue imposition on interstate commerce.

IT IS THEREFORE, ORDERED:

1. That the Respondents' Motion for an extension of time to file a counter "Proposed Order" is denied.

2. That the Commission's Order of September 2, 1981, as supplemented herein be, and the same is hereby, affirmed and sustained in all respects and is further adopted by the Full Commission as its Order.

3. That the exceptions, and each of them as filed by Nantahala, Tapoco and Alcoa be, and the same hereby are, overruled, denied and dismissed.

4. That the Stay Order issued in September 1981, pending ruling on the exceptions to the Panel's Order is vacated.

ISSUED BY ORDER OF THE COMMISSION.

This the 28th day of January 1982.

NORTH CAROLINA
UTILITIES COMMISSION

Sandra J. Webster, Chief Clerk

(SEAL)

APPENDIX E

Excerpts From The Federal Power Act,
16 U.S.C. §§ 791a–828c

Section 4, 16 U.S.C. § 797:

General powers of Commission

The Commission is authorized and empowered—

* * *

(e) **Issue of licenses for construction, etc., of dams, conduits, reservoirs, etc.**

To issue licenses to citizens of the United States, or to any association of such citizens, or to any corporation organized under the laws of the United States or any State thereof, or to any State or municipality for the purpose of constructing, operating, and maintaining dams, water conduits, reservoirs, power houses, transmission lines, or other project works necessary or convenient for the development and improvement of navigation and for the development, transmission, and utilization of power across, along, from, or in any of the streams or other bodies of water over which Congress has jurisdiction under its authority to regulate commerce with foreign nations and among the several States, or upon any part of the public lands and reservations of the United States (including the Territories), or for the purpose of utilizing the surplus water or water power from any Government dam, except as herein provided: *Provided,* That licenses shall be issued within any reservation only after a finding by the Commission that the license will not interfere or be inconsistent with the purpose for which such reservation was created or acquired, and shall be subject to and contain such conditions as the Secretary of the department under whose supervision such reservation falls shall deem necessary for the adequate protection and utilization of such reservations: *Provided further,* That no license affecting the navigable capacity of any navigable waters of the United States shall be issued until the plans of the dam or other structures affecting the navigation have been approved by the Chief of Engineers and the Secretary of the Army. Whenever the contemplated improvement is, in the judgment of the Commission, desirable and justified in

the public interest for the purpose of improving or developing a waterway or waterways for the use or benefit of interstate or foreign commerce, a finding to that effect shall be made by the Commission and shall become a part of the records of the Commission: *Provided further,* That in case the Commission shall find that any Government dam may be advantageously used by the United States for public purposes in addition to navigation, no license therefor shall be issued until two years after it shall have reported to Congress the facts and conditions relating thereto, except that this provision shall not apply to any Government dam constructed prior to June 10, 1920: *And provided further,* That upon the filing of any application for a license which has not been preceded by a preliminary permit under subsection (f) of this section, notice shall be given and published as required by the proviso of said subsection.

* * *

Section 6, 16 U.S.C. § 799:

License; duration, conditions, revocation, alteration, or surrender

Licenses under this subchapter shall be issued for a period not exceeding fifty years. Each such license shall be conditioned upon acceptance by the licensee of all of the terms and conditions of this chapter and such further conditions, if any, as the Commission shall prescribe in conformity with this chapter, which said terms and conditions and the acceptance thereof shall be expressed in said license. Licenses may be revoked only for the reasons and in the manner prescribed under the provisions of this chapter, and may be altered or surrendered only upon mutual agreement between the licensee and the Commission after thirty days' public notice. Copies of all licenses issued under the provisions of this subchapter and calling for the payment of annual charges shall be deposited with the General Accounting Office, in compliance with section 20 of title 41.

Section 10, 16 U.S.C. § 803:

Conditions of license generally

All licenses issued under this subchapter shall be on the following conditions:

(a) Modification of plans, etc., to secure adaptability of project

That the project adopted, including the maps, plans, and specifications, shall be such as in the judgment of the Commission will be best adapted to a comprehensive plan for improving or developing a waterway or waterways for the use or benefit of interstate or foreign commerce, for the improvement and utilization of water-power development, and for other beneficial public uses, including recreational purposes; and if necessary in order to secure such plan the Commission shall have authority to require the modification of any project and of the plans and specifications of the project works before approval.

* * *

Section 201, 16 U.S.C. § 824:

Declaration of policy; application of subchapter

(a) Federal regulation of transmission and sale of electric energy

It is declared that the business of transmitting and selling electric energy for ultimate distribution to the public is affected with a public interest, and that Federal regulation of matters relating to generation to the extent provided in this subchapter and subchapter III of this chapter and of that part of such business which consists of the transmission of electric energy in interstate commerce and the sale of such energy at wholesale in interstate commerce is necessary in the public interest, such Federal regulation, however, to extend only to those matters which are not subject to regulation by the States.

(b) Use or sale of electric energy in interstate commerce

(1) The provisions of this subchapter shall apply to the transmission of electric energy in interstate commerce and to the sale of electric energy at wholesale in interstate commerce, but except as provided in paragraph (2) shall not apply to any other sale of electric energy or deprive a State or State commission of its lawful authority now exercised over the exportation of hydroelectric energy which is transmitted across a State line. The Commission shall have jurisdiction over all facilities for such transmission or sale of electric energy, but shall not have jurisdiction, except as specifically provided in this subchapter and subchapter III of this chapter, over facilities used for the generation of electric energy or over facilities used in local distribution or only for the transmission of electric energy in intrastate commerce, or over facilities for the transmission of electric energy consumed wholly by the transmitter.

* * *

(c) Electric energy in interstate commerce

For the purpose of this subchapter, electric energy shall be held to be transmitted in interstate commerce if transmitted from a State and consumed at any point outside thereof; but only insofar as such transmission takes place within the United States.

(d) "Sale of electric energy at wholesale" defined

The term "sale of electric energy at wholesale" when used in this subchapter, means a sale of electric energy to any person for resale.

(e) "Public utility" defined

The term "public utility" when used in this subchapter and subchapter III of this chapter means any person who owns or operates facilities subject to the jurisdiction of the Commission under this subchapter (other than facilities subject to such jurisdiction solely by reason of section 824i, 824j, or 824k of this title).

* * *

Section 205, 16 U.S.C. § 824d:

Rates and charges; schedules; suspension of new rates; automatic adjustment clauses

(a) Just and reasonable rates

All rates and charges made, demanded, or received by any public utility for or in connection with the transmission or sale of electric energy subject to the jurisdiction of the Commission, and all rules and regulations affecting or pertaining to such rates or charges shall be just and reasonable, and any such rate or charge that is not just and reasonable is hereby declared to be unlawful.

(b) Preference or advantage unlawful

No public utility shall, with respect to any transmission or sale subject to the jurisdiction of the Commission, (1) make or grant any undue preference or advantage to any person or subject any person to any undue prejudice or disadvantage, or (2) maintain any unreasonable difference in rates, charges, service, facilities, or in any other respect, either as between localities or as between classes of service.

(c) Schedules

Under such rules and regulations as the Commission may prescribe, every public utility shall file with the Commission, within such time and in such form as the Commission may designate, and shall keep open in convenient form and place for public inspection schedules showing all rates and charges for any transmission or sale subject to the jurisdiction of the Commission, and the classifications, practices, and regulations affecting such rates and charges, together with all contracts which in any manner affect or relate to such rates, charges, classifications, and services.

(d) Notice required for rate changes

Unless the Commission otherwise orders, no change shall be made by any public utility in any such rate, charge, classification, or service, or in any rule, regulation, or contract relating thereto, except after sixty days' notice to the Commission and to the public. Such notice shall be given by filing with the Commission and keeping open for public inspection new schedules stating plainly the change or changes to be made in the schedule or schedules then in force and the time when the change or changes will go into effect. The Commission, for good cause shown, may allow changes to take effect without requiring the sixty days' notice herein provided for by an order specifying the changes so to be made and the time when they shall take effect and the manner in which they shall be filed and published.

(e) Suspension of new rates; hearings; five month period

Whenever any such new schedule is filed the Commission shall have authority, either upon complaint or upon its own initiative without complaint, at once, and, if it so orders, without answer or formal pleading by the public utility, but upon reasonable notice, to enter upon a hearing concerning the lawfulness of such rate, charge, classification, or service; and, pending such hearing and the decision thereon, the Commission, upon filing with such schedules and delivering to the public utility affected thereby a statement in writing of its reasons for such suspension, may suspend the operation of such schedule and defer the use of such rate, charge, classification, or service, but not for a longer period than five months beyond the time when it would otherwise go into effect; and after full hearings, either completed before or after the rate, charge, classification, or service goes into effect, the Commission may make such orders with reference thereto as would be proper in a proceeding initiated after it had become effective. If the proceeding has not been concluded and an order made at the expiration of such five months, the proposed change

of rate, charge, classification, or service shall go into effect at the end of such period, but in case of a proposed increased rate or charge, the Commission may by order require the interested public utility or public utilities to keep accurate account in detail of all amounts received by reason of such increase, specifying by whom and in whose behalf such amounts are paid, and upon completion of the hearing and decision may by further order require such public utility or public utilities to refund, with interest, to the persons in whose behalf such amounts were paid, such portion of such increased rates or charges as by its decision shall be found not justified. At any hearing involving a rate or charge sought to be increased, the burden of proof to show that the increased rate or charge is just and reasonable shall be upon the public utility, and the Commission shall give to the hearing and decision of such questions preference over other questions pending before it and decide the same as speedily as possible.

(f) Review of automatic adjustment clauses and public utility practices; action by Commission; definition

(1) Not later than 2 years after November 9, 1978, and not less often than every 4 years thereafter, the Commission shall make a thorough review of automatic adjustment clauses in public utility rate schedules to examine—

(A) whether or not each such clause effectively provides incentives for efficient use of resources (including economical purchase and use of fuel and electric energy), and

(B) whether any such clause reflects any costs other than costs which are—

(i) subject to periodic fluctuations and

(ii) not susceptible to precise determinations in rate cases prior to the time such costs are incurred.

Such review may take place in individual rate proceedings or in generic or other separate proceedings applicable to one or more utilities.

(2) Not less frequently than every 2 years, in rate proceedings or in generic or other separate proceedings, the Commission shall review, with respect to each public utility, practices under any automatic adjustment clauses of such utility to insure efficient use of resources (including economical purchase and use of fuel and electric energy) under such clauses.

(3) The Commission may, on its own motion or upon complaint, after an opportunity for an evidentiary hearing, order a public utility to—

(A) modify the terms and provisions of any automatic adjustment clause, or

(B) cease any practice in connection with the clause,

if such clause or practice does not result in the economical purchase and use of fuel, electric energy, or other items, the cost of which is included in any rate schedule under an automatic adjustment clause.

(4) As used in this subsection, the term "automatic adjustment clause" means a provision of a rate schedule which provides for increases or decreases (or both), without prior hearing, in rates reflecting increases or decreases (or both) in costs incurred by an electric utility. Such term does not include any rate which takes effect subject to refund and subject to a later determination of the appropriate amount of such rate.

Section 206, 16 U.S.C. § 824e:

Power of Commission to fix rates and charges; determination of cost of production or transmission

(a) Unjust or preferential rates, etc.

Whenever the Commission, after a hearing had upon its own motion or upon complaint, shall find that any rate, charge, or classification, demanded, observed, charged, or collected by any

public utility for any transmission or sale subject to the jurisdiction of the Commission, or that any rule, regulation, practice, or contract affected such rate, charge, or classification is injust, unreasonable, unduly discriminatory or preferential, the Commission shall determine the just and reasonable rate, charge, classification, rule, regulation, practice, or contract to be thereafter observed and in force, and shall fix the same by order.

(b) Investigation of costs

The Commission upon its own motion, or upon the request of any State commission whenever it can do so without prejudice to the efficient and proper conduct of its affairs, may investigate and determine the cost of the production or transmission of electric energy by means of facilities under the jurisdiction of the Commission in cases where the Commission has no authority to establish a rate governing the sale of such energy.

Section 306, 16 U.S.C. § 825e:

Any person, State, municipality, or State commission complaining of anything done or omitted to be done by any licensee or public utility in contravention of the provisions of this chapter may apply to the Commission by petition which shall briefly state the facts, whereupon a statement of the complaint thus made shall be forwarded by the Commission to such licensee or public utility, who shall be called upon to satisfy the complaint or to answer the same in writing within a reasonable time to be specified by the Commission. If such licensee or public utility shall not satisfy the complaint within the time specified or there shall appear to be any reasonable ground for investigating such complaint, it shall be the duty of the Commission to investigate the matters complained of in such manner and by such means as it shall find proper.

APPENDIX F

Excerpts From The North Carolina Public Utilities Act, N.C. Gen. Stat. §§ 62-1, *et seq.*

§ 62-133. How rates fixed.

(a) In fixing the rates for any public utility subject to the provisions of this Chapter, other than motor carriers and certain water and sewer utilities, the Commission shall fix such rates as shall be fair both to the public utility and to the consumer.

(b) In fixing such rates, the Commission shall:

(1) Ascertain the reasonable original cost of the public utility's property used and useful, or to be used and useful within a reasonable time after the test period, in providing the service rendered to the public within this State, less than portion of the cost which has been consumed by previous use recovered by depreciation expense plus the reasonable original cost of investment in plant under construction (construction work in progress). In ascertaining the cost of the public utility's property, construction work in progress as of the effective date of this subsection shall be excluded until such plant comes into service but reasonable and prudent expenditures for construction work in progress after the effective date of this subsection may be included, to the extent the Commission considers such inclusion in the public interest and necessary to the financial stability of the utility in question, subject to the provisions of subparagraph (b)(5) of this section.

(2) Estimate such public utility's revenue under the present and proposed rates.

(3) Ascertain such public utility's reasonable operating expenses, including actual investment currently consumed through reasonable actual depreciation.

(4) Fix such rate of return on the cost of the property ascertained pursuant to subdivision (1) as will enable the public utility by sound management to produce a fair return for its shareholders, considering changing economic conditions and other factors, as they then exist, to maintain its facilities and services in accordance with the reasonable requirements of its customers in the territory covered by its franchise, and to compete in the market for capital funds on terms which

are reasonable and which are fair to its customers and to its existing investors.

(4a) Require each public utility to discontinue capitalization of the composite carrying cost of capital funds used to finance construction (allowance for funds) on the construction work in progress included in its rate based upon the effective date of the first and each subsequent general rate order issued with respect to it after the effective date of this subsection; allowance for funds may be capitalized with respect to expenditures for construction work in progress not included in the utility's property upon which the rates were fixed. In determining net operating income for return, the Commission shall not include any capitalized allowance for funds used during construction on the construction work in progress included in the utility's rate base.

(5) Fix such rates to be charged by the public utility as will earn in addition to reasonable operating expenses ascertained pursuant to subdivision (3) of this subsection the rate of return fixed pursuant to subdivisions (4) and (4a) on the cost of the public utility's property ascertained pursuant to subdivision (1).

(c) The original cost of the public utility's property, including its construction work in progress, shall be determined as of the end of the test period used in the hearing and the probable future revenues and expenses shall be based on the plant and equipment in operation at that time. The test period shall consist of 12 months' historical operating experience prior to the date the rates are proposed to become effective, but the Commission shall consider such relevant, material and competent evidence as may be offered by any party to the proceeding tending to show actual changes in costs, revenues or the cost of the public utility's property used and useful, or to be used and useful within a reasonable time after the test period, in providing the service rendered to the public within this State, including its construction work in progress, which is based upon circumstances and events occurring up to the time the hearing is closed.

(d) The Commission shall consider all other material facts of record that will enable it to determine what are reasonable and just rates.

(e) The fixing of a rate of return shall not bar the fixing of a different rate of return in a subsequent proceeding.

(f) Unless otherwise ordered by the Commission subsections (b), (c), and (d) shall not apply to rate changes of utilities engaged in the distribution of natural gas bought at wholesale by the utility for distribution to consumers to the extent such rate changes are occasioned by changes in the wholesale rate of such natural gas. The Commission may permit such rate changes to become effective simultaneously with the effective date of the change in the wholesale cost of such natural gas, or at such other time as the Commission may direct. This subsection shall not prohibit the Commission from investigating and changing unreasonable rates in accordance with the provisions of this Chapter. The public utility shall give such notice, which may include notice by publication, of the changes to interested parties as the Commission in its discretion may direct.

(g) Reserved.

(h) The Commission is not authorized to entertain applications filed on behalf of intrastate rail carriers to fix rates for a single commodity or to fix rates for groups of commodities which constitute less than a general rate increase.

APPENDIX G

Opinion Of FERC In *Tapoco, Inc.*,
Docket No. ER81-19-000

Tapoco, Inc., Docket No. ER81-19-000

Order Declaring Jurisdiction, Accepting Agreement for Filing Subject tó Outcome of Other Proceedings, Waiving Notice and Additional Filing Requirements, Granting Intervention, and Terminating Docket

(Issued December 2, 1980)

Before Commissioners: Charles B. Curtis, Chairman; Matthew Holden, Jr., George R. Hall and J. David Hughes.

On October 9, 1980, Tapoco, Inc. (Tapoco) tendered for filing, pursuant to section 35.12 of the Commission's regulations, an apportionment agreement with Nantahala Power and Light Company (NP&L) dated June 1, 1971,[1] which arose out of a December 27, 1962 agreement entitled the New Fontana Agreement (NFA).

The NFA, which is on file as Tapoco's Rate Schedule No. 3, provides for an energy-for-energy swap by Tapoco and NP&L, both subsidiaries of Alcoa, with the Tennessee Valley Authority (TVA). Under the NFA, the energy generated by Tapoco and NP&L is dispatched by and delivered to TVA which, in return, provides Tapoco and NP&L with a fixed annual entitlement of power to be delivered at specified points.

The apportionment agreement is an adjunct to the NFA, specifying the amounts of TVA energy to which NP&L and Tapoco are entitled. While the NFA has been on file with the Commission, the 1971 apportionment agreement has not. In consolidated Docket Nos. EL78-18 and EL78-828,[2] the Commission staff expressed the position that Commission regulations mandated the filing of the apportionment agreement on the grounds that

[1] Designated as Supplement No. 2 to Tapoco Rate Schedule FPC No. 3.

[2] Docket No. EL78-18 is a complaint proceeding initiated by the Town of Highlands, North Carolina. Docket No. ER76-828 is a proceeding instituted to consider proposed wholesale rates filed by NP&L.

it is a jurisdictional rate schedule and an integral portion of the NFA. Tapoco indicates in its transmittal letter that it is cognizant of the broad definition of "rate schedule" under the Federal Power Act as set forth in 35.2 of the regulations, and that it therefore has chosen not to contest the issue and has tendered the instant filing. However, Tapoco further states, somewhat inconsistently, that it is submitting the apportionment agreement under protest "because of the potential conflicting jurisdictional assertions by the Commission and the Tennessee Valley Authority."

Tapoco requests that the Commission find the agreement to be non-jurisdictional, asserting that no rates, charges or jurisdictional services are specified therein. Moreover, Tapoco requests waiver of any additional filing requirements contemplated by the Commission's regulations on the grounds that the agreement does not provide for any service to be rendered by Tapoco and that the terms and conditions of the instant submittal have been litigated in Docket Nos. ER76-828 and EL78-18.

Notice of the filing was issued on October 21, 1980, with comments, protests, or petitions to intervene due on or before November 10, 1980. The Town of Highlands, North Carolina, a wholesale customer of NP&L, filed a protest and petition to intervene on November 10, 1980, primarily aimed at preserving its position in Docket Nos. EL78-18 and ER76-828. Highlands indicates that the instant agreement has been the subject of extensive litigation and that relitigation in the instant docket should be avoided. Highlands requests that the agreement be accepted for filing, that a determination be made that the submittal is jurisdictional, that Tapoco be required to file data in support of the power allotments contained in the filing, and that the submittal be suspended for five months from the filing of such data.

Highlands states that its principal areas of concern are: (1) the assurance that any action taken with respect to the instant docket will not prejudice its position or right to refunds in Docket Nos.

EL78-18 and ER76-828; and (2) the preservation of Commission authority to order appropriate modifications to the instant agreement upon final disposition of Docket Nos. EL78-18 and ER76-828.

Discussion

The Commission notes that the apportionment agreement is an integral part of the NFA designed to implement the provisions of the NFA. As indicated above, the NFA is a jurisdictional rate schedule on file with the Commission. Accordingly, the Commission concludes that the apportionment agreement, as a contract relating to and affecting operation of a filed rate schedule, is itself a jurisdictional rate schedule which should appropriately be filed as a supplement to the NFA. We further observe, however, that the issue of the proper apportionment of TVA power between NP&L and Tapoco is a subject which has been fully litigated and is awaiting initial decision in Docket Nos. ER76-828 and EL78-18. Therefore, the Commission will declare the apportionment agreement to be jurisdictional, and will waive outstanding filing requirements and accept the agreement for filing to become effective on June 1, 1971, when service commenced under the agreement. While we shall terminate the instant docket, the apportionment question shall remain subject to the outcome of the proceedings in Docket Nos. ER76-828 and EL78-18. In addition, we shall require NP&L to submit an appropriate certificate of concurrence which will also become effective as of June 1, 1971, subject to the outcome of the prior dockets.[3]

We believe that this procedure will preserve the interests of all affected parties, while avoiding unnecessary duplication of litigation. With respect to the apportionment issue, NP&L's wholesale customers will be protected in the event than any change is required in the allocation of costs between Tapoco and NP&L by

[3]NP&L has indicated that it challenges the jurisdictionality of the NFA, but that it will comply with applicable Commission directives.

means of the refund provision as stipulated in Docket Nos. EL78-18, ER76-828, and ER80-574.[4]

The Commission finds that participation in this proceeding by Highlands may be in the public interest. Accordingly, we shall grant Highlands' petition to intervene in this docket.

The Commission orders:

(A) The instant submittal is hereby declared to be jurisdictional and is accepted for filing to be effective as of June 1, 1971, *provided, however,* that the reasonableness of the apportionment arrangement shall be subject to the outcome of the proceedings in Docket Nos. EL78-18 and ER76-828, and subject to the refund provisions therein.

(B) The notice requirements of the Commission's regulations are hereby waived.

(C) Tapoco's request for waiver of additional filing requirements is hereby granted.

(D) NP&L is hereby directed within 30 days of the issuance of this order to file a certificate of concurrence with the apportionment agreement, which, upon filing, shall become effective as of June 1, 1971, subject to the outcome of Docket Nos. ER76-828 and EL78-18.

(E) Highland's petition to intervene is hereby granted, subject to the rules and regulations of the Commission; *provided, however,* that participation by the intervenor shall be limited to matters set forth in its petition to intervene; and *provided, further,* that the admission of this intervenor shall not be construed as recognition by the Commission that it might be aggrieved because of any order or orders by the Commission entered in this proceeding.

(F) Docket No. ER81-19-000 is hereby terminated.

(G) The Secretary shall promptly publish this order in the Federal Register.

[4]Docket No. ER80-574 involves NP&L's most recent wholesale rate change case.

APPENDIX H

Excerpts from Administrative Law Judge Decision,
Nantahala Power and Light Company,
Docket No. ER76-828;
Town of Highlands, North Carolina
v. *Nantahala Power and Light Company,*
Docket No. EL78-18;

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Nantahala Power and Light Company, Docket No. ER76-828; Town of Highlands, North Carolina, *et al.* v. Nantahala Power and Light Company, Docket No. EL78-18

Initial Decision

(Issued April 10, 1981)

Jacob Leventhal, Administrative Law Judge.

TABLE OF CONTENTS

Procedural History ....
Preliminary Matter ....
I. Docket No. EL78-18, the Complaint Proceedings ....
Ruling ....
II. Purchased Power Adjustment Clause (PPAC) ......
1. Position of Nantahala ....
2. Position of Commission Staff ....
3. Highlands' Position ....
Ruling ....
III. Synchronization of Interest Expense ....
Ruling ....
IV. Revised Regulatory Expense ....
Ruling ....
V. Functionalization of Plan ....
Ruling ....
VI. Cash Working Capital ....
Ruling ....
VII. Allocation of Transmission Costs ....
Ruling ....
VIII. Classification of Hydro Investment ....
Ruling ....
IX. Demand Cost Allocation ....
X. Rate of Return ....
A. Capital Structure ....
B. Other Items of Capital ....

C. Overall Rate of Return ....
Ruling ....
XI. Commission's Authority to Accept Nantahala's Filing
Ruling ....
XII. Restatement of Wartime Depreciation ....
Ruling ....
Ultimate Findings and Conclusions ....
Order ....
Footnotes ....

Procedural History

On July 30, 1976, Nantahala Power and Light Company (Nantahala) tendered for filing proposed tariff provisions which provided for increased annual charges of $121,908 (28.2%) based on the test period ending December 31, 1975. The rate increase affects three wholesale customers, Haywood Electric Membership Corporation (Haywood), the Town of Highlands, North Carolina (Highlands) and Western Carolina University.

By order issued August 31, 1976, the Commission accepted the proposed increase for filing, subject to refund, suspended its effectiveness until October 1, 1976 and set the matter for hearing.

Petitions to intervene filed by North Carolina Electric Membership Corporation (NCEMC), Haywood and Highlands were granted.

The first prehearing conference was held on May 10, 1976. At that time Nantahala requested additional time to develop a cost of service rate to present in Docket E-9181, a related rate case. No further conferences were held until May, 1978.

On April 24, 1978 Highlands filed a complaint pursuant to Section 306 of the Federal Power Act against Nantahala, Tapoco, Inc. (TAPOCO) and the Aluminum Company of America

(Alcoa) in Docket No. EL78-18. The complaint alleged that Nantahala's rates are too high because of allegedly illegal activities engaged in by Alcoa. NCEMC and Haywood petitioned to intervene, in support of the complaint on June 9, 1978. The petition was granted and they filed an answer on July 10, 1978.

Docket EL78-18 was consolidated with the rate docket on motion of Highlands. A second prehearing conference was held on May 10, 1978. Thereafter there was extensive prehearing practice involving a number of motions with the attendant submission of briefs and oral arguments. Twenty-two days of hearing were held between April 8 and May 8, 1980. Initial and reply briefs were filed June 26 and July 31, 1981 respectively.

Because of the retirement and subsequent death of Presiding Judge Graham McGowan, this proceeding was assigned to me for determination. A final oral argument on the issues was held before me on October 17, 1980 and the parties filed indices to their respective briefs on October 28, 1980.

* * *

I. Docket No. EL78-18 The Complaint Proceedings

The complainants contend that Alcoa, through the guise of co-respondents Tapoco, and Nantahala, has violated the Federal Power Act by diverting facilities formerly dedicated to public service to its private use and benefit at the expense of Nantahala's ratepayers. In particular, Highlands alleges that Alcoa has: (1) assigned the best hydro-electric generating facilities in the western North Carolina region to its own service through Tapoco, Inc. and Tapoco's predecessors, while leaving Nantahala with facilities claimed to be more costly; (2) caused Nantahala to relinquish assets and contractual obligations for the benefit of Alcoa without receiving consideration in return; and (3) caused Nantahala to receive less than a reasonable share of the benefits arising from the New Fontana agreement.

In order to understand the nature of these allegations, a short synopsis of the various contractual agreements must be set forth.

1. Original Fontana Agreement (Tapoco Exh. 6) (August 14, 1941). A twenty year agreement between Alcoa and TVA which turned over land owned by Nantahala and Tapoco to TVA for the purpose of developing the Fontana Dam. This contract also provided that all of the generation of Nantahala's plants (with the exception of three small plants) and Tapoco's plants and effective control of two generating systems be turned over to TVA in return for a specified amount of power, 218.3 Mw.

2. New Fontana Agreement (Exh. of Answer) (December 27, 1962). This contract was similar to the prior agreement and continued some of its provisions. It changed the amount of entitlements from TVA to Nantahala, Tapoco and Alcoa. It was signed by all four parties, Alcoa, Tapoco, Nantahala and TVA.

3. 1963 Apportionment Agreement (Nantahala Exh. 42) (January 1, 1963). This was an agreement between Nantahala and Alcoa which divided, between the two utilities, the entitlements from the New Fontana Agreement. Nantahala received, each month, $^1/_{12}$ of its annual primary energy capability of 360,000,000 kwh or its actual generation and $89,200 per year from Alcoa for allowing TVA to operate its projects. In this and the following agreement, the balance of the entitlements go to Tapoco.

4. 1971 Apportionment Agreement (Nantahala Exh. 44) (June 1, 1971). Essentially a revision of the allocations made in the 1963 contract. Alcoa was not a party to this contract. Nantahala's energy entitlement was fixed at 360,000,000 kwh annually and its capacity limitation was 54.3 Mw. The $89,200 payment was not mentioned and hence terminated.

A brief history of the operations of Alcoa and its electric power subsidiaries will clarify the allegations of the compaint.

Alcoa conducts aluminum smelting operations in the town of Alcoa, Tennessee. As aluminum smelting is a process requiring large amounts of energy, Alcoa has, over the past years, set up

corporate subsidiaries which generate electricity and sell it to Alcoa. They are Tapoco, Nantahala, and Carolina Aluminum Company.

Tapoco is the current name of what was originally the Knoxville Power Company. Incorporated in the State of Tennessee in 1900, the company was acquired by Alcoa in 1910, and its primary function until 1945 was to service a public load in Blount County, Tennessee with power purchased from other companies. In 1927, Knoxville Power Company began construction of the Calderwood hydro facility on the Little Tennessee River which was transferred in 1929 to Alcoa upon the order of the Tennessee Railroad and Public Utilities Commission. In approving the transfer, the Tennessee Commission explicitly noted the intention of Knoxville and Alcoa that all power and energy produced at the Calderwood facility be used by Alcoa in its Tennessee smelting operations (Tapoco Exh. 11, pp. 1-2; Tr. 2634). Operations of the Calderwood facility began in 1930 and, in 1945, the project was reacquired by Knoxville from its parent company.

In 1954, Knoxville Power changed its name to Tapoco, Inc. The following year the company obtained a certificate of public convenience and necessity from the Tennessee authorities for the construction of the Chilhowee hydro project, also located on the Little Tennessee River and the Federal Power Commission issued a joint license to Tapoco and Carolina Aluminum Company to operate the Calderwood facilities, plus the existing Cheoah and Santeetlah hydro facilities. Later in 1955, Tapoco acquired these last two developments from Carolina Aluminum and transmission facilities from Nantahala, consisting of a line from the Santeetlah facility to the North Carolina-Tennessee border. Also that year, Tapoco sold its distribution system and public service franchise to the City of Blount, Tennessee. As a result, Tapoco's output has, since 1955, been entirely dedicated to Alcoa's smelting operations. The company has not been regulated by either the Tennessee Public Service Commission or the North Carolina

Public Utilities Commission. However, in 1954, Tapoco was domesticated in North Carolina (Tapoco Exhibit 17) in connection with its application to acquire the Santeetlah and Cheoah projects. Tapoco is a "licensee" under Title I of the Federal Power Act and a "public utility" within the scope of Title II of the Act. Accordingly, the company's power sales agreement with Alcoa is on file with this Commission.

Nantahala was incorporated in North Carolina in 1929 and has been subject to regulation by the North Carolina Public Utilities Commission as well as this Commission and its predecessor, the Federal Power Commission (FPC). The company serves six counties in western North Carolina and has as its primary resource eleven hydro generating plants, ten of which are located on the Little Tennessee River. As a result of the increase in demand that occurred in World War II, Alcoa commenced the purchase of power from Nantahala, which constructed the Nantahala and Thorpe projects primarily to meet this increase in demand. Originally, the hydroelectric facilities were constructed after filing applications with the FPC, which determined that no license was required. In 1966, the FPC reversed its prior findings. See 36 F.P.C. 119 (1966). These sales to Alcoa ceased in 1971 as a result of the increase over the years placed upon Nantahala by other public load customers.

A third power company, Carolina Aluminum Company, should be mentioned. Chartered in North Carolina in 1905, the company was originally known as the Tallahassee Power Company (Tallahassee) and its purposes included the development and supply of public and private loads, both in North Carolina and out-of-state. Alcoa acquired Tallahassee in 1911. Its principal activities included acquisition of land rights to develop the Cheoah project, completed in 1919, and the Santeetlah project, which was completed and commenced service in 1929. The construction of the latter project included the use of eminent domain and culminated in one court decision, ***Whiting Manufacturing v. Carolina Alumi-***

num Company, 207 N.C. 52, 175 S.E. 698 (1934). The bulk of the power generated at the Cheoah and Santeetlah plants was transmitted to Knoxville Power Co. for delivery to Alcoa. In 1929, Tallahassee sold its undeveloped power sites in western North Carolina to Nantahala. In 1931, the company changed its name to Carolina Aluminum Company and, in 1955, sold the Cheoah and Santeetlah developments to Tapoco, Inc.

As indicated, practically all the hydroelectric facilities owned by Nantahala and Tapoco are located on the Little Tennessee River. Separating the two companies' generation sites is the Fontana project; Nantahala's hydro projects are all located upstream of the Fontana dam, while Tapoco's are all downstream.

The Fontana hydro project was developed by the Tennessee Valley Authority (TVA). Originally, Nantahala desired to develop the Fontana Site, as evidenced by its declaration of intention to the FPC in October, 1940. See *Nantahala Power & Light Company*, 2 F.P.C. 833 (1940). Subsequent to the Commission's decision that a license would be required for the Fontana dam, while Tapoco's are all downstream.

The Fontana hydro project was developed by the Tennessee Valley Authority (TVA). Originally, Nantahala desired to develop the Fontana Site, as evidenced by its declaration of intention to the FPC in October, 1940. See *Nantahala Power & Light Company*, 2 F.P.C. 833 (1940). Subsequent to the Commission's decision that a license would be required for the Fontana dam, the plans to go ahead were dropped. Instead, the original Fontana agreement was executed in 1941 by TVA and Alcoa. The original Fontana agreement was superseded by the New Fontana Agreement (NFA) which became effective on January 1, 1963. Since neither of these agreements specified how the power and energy were to be divided as between the two Alcoa subsidiaries, the two apportionment agreements were executed. The 1963 one was never filed with the FPC and the 1971 agreement was finally

filed in 1980. Additional power and energy necessary to serve Nantahala's public load is purchased from TVA.

Highlands' position is that Alcoa's control of Nantahala and Tapoco has been used to obtain power at a low cost to the detriment of Nantahala's customers. Highlands proposes several remedies. First, it asks that the corporate veil between the two utilities be pierced and that they be considered one entity for ratemaking purposes. The cost of service should be established on a rolled-in basis of the combined power systems. Second, Highlands requests that the 1971 Apportionment Agreement be reformed to reflect a more fair and reasonable allocation of power and energy to Nantahala. Finally, it asserts that all of the agreements not currently filed be filed with this Commission.

Ruling

* * *

Highlands has not sustained its burden of proof on the issue of piercing the corporate veil and combining the two utilities for rate making purposes. Nantahala and Tapoco are separate entities. They were chartered in separate states; were developed separately; served separate customer loads; are not integrated except as part of the TVA system; are interconnected at only one point; and have separate corporate headquarters.

Whether Tapoco is recognized as a public utility by the Supreme Court of the State of North Carolina is not determinative of the issue before this Commission.

The substance of the complaint is that Highlands alleges an unfair and unjust allocation of power and facilities under the various agreements. To remedy this situation, it is not necessary to pierce the corporate veil. As discussed below, a more appropriate relief is available. This relief is to set rates for Nantahala as if the 1971 Apportionment Agreement were reformed to reflect a fair allocation of power and energy to Nantahala.

Highlands, in its complaint, and staff, in its brief, aver that the 1971 Apportionment Agreement is not fair and reasonable to Nantahala. It is Highlands' position that both the capacity and energy allocations are unfair while staff argues that this is true only with respect to the energy allocations. Their positions regarding the other agreements also differ.

Staff asserts that only the 1971 agreement is unfair. They agree with the respondents that the New Fontana Agreement (NFA) was negotiated at arms-length and is fair and reasonable. (R.B. at 14-16) According to staff, the record supports the respondents' argument that Nantahala was adequately compensated for that which it gave to TVA and its interests were protected during the negotiations. This, staff asserts, is not true of the 1971 agreement. Mr. Foreman, staff's witness, testified that Nantahala's share of the energy entitlements flowing from NFA are not proportional to the energy it turns over to TVA under NFA. It is his position that Nantahala's rates should be set as if it were receiving a larger share of the energy. Staff also argues that since the 1971 agreement is a contract affecting rates, it should have been filed with the Commission when made and the failure to make a timely filing should result in the imposition of sanctions. (Tr. 3534)

Highlands' position encompasses that of staff and goes well beyond it. Specifically, Highlands argues that the entitlements from NFA are designed to meet Alcoa's needs and that the lion's share of those entitlements are allocated to Tapoco, Alcoa's electric supplier, under the 1971 Apportionment Agreement. They cite to numerous documents which allegedly show that the primary concern during the negotiations for the agreements was to assure that Alcoa would have an adequate supply of power. This latter point is also argued with respect to the original Fontana Agreement and the 1963 Apportionment Agreement, although both of them have been superseded by the two later agreements. As does staff, Highlands avers that the filing issue is not moot. It takes the position that the lack of a timely filing gives

rise to a presumption that the 1971 Agreement was not fair and reasonable. (R.B. pp. 15-17)

All of these issues are contested by the Respondents. They contend that the 1971 Agreement cannot be reformed for two reasons. First, this is a contract which, under the *Mobile-Sierra* doctrine, cannot be altered except after a showing that it is not in the public interest, and neither staff nor Highlands has made this showing. Additionally, even if such a showing is made, the contract may only be modified prospectively. (R.B. p. 5-7) Secondly, since the entitlements being allocated under the agreement are fixed by the NFA, any increase in Nantahala's share will necessarily decrease Tapoco's share. Thus, even if Nantahala did not receive all that it is entitled to, there is no showing that Tapoco has received more than its share or even that it has obtained its fair share. Correcting an alleged injustice to Nantahala by doing a wrong to Tapoco is wholly improper.

The respondents hold that staff's position is analytically flawed in that their witness fails to properly distinguish the different types of power to be allocated. This, they contend, is also true of Highlands' witness, Mr. Springs. As to Highlands' arguments directed toward the negotiations for the above agreements, the Respondents assert that these arguments are nothing more than a negative inference which does not satisfy the burden of proof Highlands has in its position as a complainant. Moreover, regardless of what occurred during the negotiations, the end result is not unfair to Nantahala or its ratepayers. Finally, the respondents assert that the filing issue is moot since the 1971 Agreement has been filed with the Commission.

The first issue to be dealt with is the filing issue. There can be no question that the 1971 Apportionment Agreement is a contract affecting, in some manner, rates and charges under § 205(c) of the Federal Power Act and should have been filed when made.[1]

[1]16 USC 824d(c), Regs. § § 35.1 & 2.

However, Nantahala's failure to make a timely filing does not give rise to any sanctions assessable by an administrative law judge. Nor does that failure give rise to a presumption that the 1971 agreement is unreasonable. The respondents are not, as Highlands argues, placed in a better position by their failure to file than if they had filed. Even if the agreements had been filed, Highlands, as a complainant, would still need to establish its *prima facie* case and the respondents would still have the ultimate burden of persuasion.

The next issue is the alleged unfairness of the 1971 Apportionment Agreement. In its brief, Highlands attacks all four of the agreements listed at the outset of this discussion as unfair and unreasonable. Although the original Fontana Agreement and the 1963 Apportionment Contract have been superseded, Highlands argues that they are unfair and unreasonable apparently to demonstrate the continuing nature of the alleged improprieties with regard to Nantahala and also because there is a carry-over of some of the provisions of the two prior agreements to the current agreements. However, those arguments relate to its requested relief that Nantahala and Tapoco be combined. Since that relief has been ruled inappropriate, the remaining discussion will be limited to the 1971 agreement.

According to Highlands and staff, the 1971 Apportionment Agreement should have allocated the power available from TVA under NFA according to each utility's proportionate contribution to the power made available to TVA, but, instead, it gave too little power to Nantahala. Respondents submit a study (Apportionment Study) which they allege is the basis of the 1971 Agreement and demonstrates the fairness of that contract. However, there is a substantial amount of evidence showing that the respondents' position is untenable.

Probably the strongest evidence relates to the fact that the 1963 Agreement, which was supposed to be effective for the term

of NFA, was superseded by the 1971 Agreement. Staff's witness, Mr. Foreman and Highlands' witness, Mr. Springs, agree that the earlier agreement provided greater benefits to Nantahala, (Tr. 3310-34; 1961 respectively) such as the $89,200 payment by Alcoa. Yet the respondents offer no evidence as to what Nantahala received in exchange for surrendering its rights under the 1963 contract for the less favorable 1971 Agreement. The respondents defend Nantahala's agreeing to the later contract on the grounds that the earlier contract was rendered moot by the North Carolina Utilities Commission. (Tr. 1389) However, a reading of the decision of the State Commission and the testimony of Nantahala's witness shows that only a part of that contract was affected by the State Commission's decision. The allotment of power was unaffected. Additionally, Mr. Foreman testified that Alcoa and Nantahala continued to abide by the terms of that agreement after it was allegedly nullified by the State Commission. (Tr. 3312) Hence, it must be concluded that the evidence shows that Nantahala, without any compensation, gave up its rights under the 1963 Agreement.

Mr. Foreman and Mr. Springs also attempt to show that the 1971 Apportionment Agreement is unfair in that Nantahala is not allocated the proper share of the NFA power. Mr. Springs' analysis is essentially a comparison of Nantahala's generating capability and its share of power and energy under the 1971 contract. He argues that since the former is less than the latter, the agreement is not fair. (Tr. 1956-59) The problem with his analysis is that it ignores any trade-offs in the NFA. That is, under the NFA, the two utilities receive less power and energy than they turn over to TVA ostensibly because of other benefits derived from TVA, such as downstream benefits. Since the NFA entitlements are not equal to the total of the generation of the two utilities, Nantahala should not be allocated its generation as its share of the NFA entitlements. Thus, Mr. Springs' proposed allocation must be rejected.

Mr. Foreman's analysis and recommended allocation is more reasonable. His proposed allocation to Nantahala is that portion of the NFA entitlements which is proportionate to Nantahala's contribution to the power turned over to TVA. (Tr. 3316-17) That is, he finds that Nantahala's potential energy generation is 22.5% of the potential energy generation turned over to TVA and therefore Nantahala should be allocated 22.5% of the energy entitlements under NFA, or 404,268,300 kwh. (Tr. 3325) His analysis also shows that Nantahala's capacity credit should be 68.3MW. (Tr. 3327) He recommends that rates be set accordingly and, after the 1971 Agreement is filed, that it be reformed to reflect these changes.

Respondents take issue with Mr. Foreman's calculations. They argue that if Nantahala should get a certain percentage of the NFA entitlements, then it should take that percentage of uninterruptible and interruptible energy and Nantahala should not first take all of the uninterruptible energy. If Mr. Foreman were consistent, they argue, the cost of purchased power would actually be far greater than its present level since all of the interruptible energy would need to be firmed up. (R.B. pp. 7-12) They also assert that the *Mobile-Sierra* doctrine prevents any change in the contracts. (R.B. 5-7)

The respondents' *Mobile-Sierra* argument misinterprets that doctrine. Those cases applied only to contracts in which the rates were set, not to contracts whose costs may be flowed through to the ratepayers. If their argument were accepted, then any agreement whose costs affect a utility's rates (e.g. fuel supply contracts, construction contracts) could not be reviewed except under § 206. This is not the import of that doctrine, and, therefore, this argument must be rejected.

Similarly, the respondents' other argument must also be rejected. Essentially they assert that Mr. Foreman ignores the distinction between primary and secondary power. Yet they accepted his

definitions when they cited, with approval, the staff's position on the fairness of the NFA. (R.B. p. 40) Staff's position there was also based on Mr. Foreman's analysis. Moreover, this distinction was apparently considered unimportant by Alcoa under the 1963 Apportionment Contract where Nantahala was entitled to a varying amount of energy dependent on its actual generation. That contract would have allowed Nantahala to be credited for an amount of energy greater than the 360 Mw of *uninterruptible* energy available under NFA. (Nantahala Ex. 42, p. 2) Finally, respondents' argument that Nantahala received all of the "primary" energy and none of the secondary energy because it could only use the former and not the latter without firming it up (R.B. pp. 9-13) would mean that there could not have been any meaningful negotiation in the 1971 agreement because the parties were already locked-in to an allocation due to the nature of the NFA entitlements. Since the respondents contend, in effect, that the 1971 contract was a bargained for exchange, there had to have been room to negotiate. Hence, their arguments show a good deal of inconsistency. The record supports Mr. Foreman's allocation and the rates should be set as if that were the allocation used.

The respondents are correct in asserting that the 1971 contract may not be reformed. Although there is ample evidence in the record demonstrating that Nantahala was not accorded its fair share of the power, there is little convincing evidence that Tapoco unfairly benefitted from that misallocation of power. Mr. Springs attempted to do this, but his analysis is so closely tied in with his argument that the two utilities should be combined that the two positions cannot clearly be separated. Thus, Highlands has not even made out a *prima facie* case for reformation.

Therefore, the rates should be set as if the 1971 Agreement allocated the NFA entitlements as Mr. Foreman proposed, but the agreement should not be reformed.

* * *

Ultimate Findings and Conclusions

Upon consideration of the record in this proceeding, I find that:

1. Nantahala Power and Light Company is a public utility under the Federal Power Act.

2. The proposals at issue involve sales of electric power at wholesale in interstate commerce and are subject to the jurisdiction of this Commission.

3. The changes in rates and charges, except to the extent heretofore specifically approved, have not been shown to be just and reasonable and they are found to be excessive or otherwise unlawful.

4. The just and reasonable rates and charges are those which are in conformity with the findings and conclusions set forth in this decision.

5. Nantahala is required to refund to its jurisdictional customers any amounts reflecting the difference between its proposed rates and the rates found just and reasonable pursuant to this decision.

6. Any relief requested in the complaint proceedings not specifically granted is denied.

* * *

APPENDIX I

Excerpts From FERC Opinion No. 139,
Nantahala Power and Light Company,
Docket No. ER76-828-000;
Town of Highlands, North Carolina
v. *Nantahala Power and Light Company,*
Docket No. EL78-18-000

Nantahala Power and Light Company, Docket No. ER76-828-000

Town of Highlands, North Carolina, et al. v. Nantahala Power and Light Company, Docket NO. EL78-18-000

Opinion NO. 139, Opinion and Order Modifying Initial Decision

(Issued May 14, 1982)

Before Commissioners: C.M. Butler III, Chairman; Georgiana Sheldon, J. David Hughes and A.G. Sousa.

This consolidated proceeding involves a July 30, 1976 rate increase filing by Nantahala Power and Light Company (Nantahala) and an April 24, 1978 complaint filing pursuant to Section 306 of the Federal Power Act by the Town of Highlands, North Carolina (Highlands). The matters were consolidated by the Commission on November 22, 1978, because certain issues of corporate misuse were raised by Highlands in both proceedings.

In Docket No. ER76-828, Nantahala seeks an annual rate increase of $121,908 (28.2%) to three wholesale customers: Highlands, Haywood Electric Membership Corporation (Haywood), and Western Carolina University. The proposed rates are based on the test period ending December 31, 1975. They are effective, subject to refund, for the locked-in period October 1, 1976 to March 1, 1981.

In Docket No. EL78-18, Highlands alleges that Aluminum Company of America (Alcoa) and its wholly owned subsidiaries, Nantahala and Tapoco, Inc. (Tapoco), are in violation of the Federal Power Act by diverting, for the benefit and private use of Alcoa, hydroelectric power and facilities dedicated to public service. Highlands is supported in its complaint by Haywood and the Attorney General of the State of North Carolina (Complainants/Intervenors).

The numerous issues raised in these proceedings were heard in April and May 1980, by Presiding Judge Graham McGowan,

who retired and died prior to a determination of the issues. Judge Jacob Leventhal was assigned to the dockets and heard a final oral argument on the issues October 17, 1980. He issued an initial decision April 10, 1981.

Briefs on and opposing exceptions to the initial decision have been filed by the Commission staff, Nantahala, Complainants/Intervenors, Tapoco and Alcoa. The issues raised in the exceptions included demand cost allocation, cash working capital, purchased power adjustment clause, rate of return, restatement of depreciation charges, and numerous substantive and procedural matters raised in the complaint proceeding.

Based on the record evidence, we affirm and adopt the initial decision on all issues except rate of return.

I. Docket No. EL78-18 Complaint Proceeding

A. *Background*

At issue in this complaint proceeding is the appropriate allocation of costs associated with certain hydroelectric developments along the Little Tennessee River. The flow of the Little Tennessee River is regulated by the Tennessee Valley Authority (TVA) through the Fontana Dam, which was developed by TVA in the 1940's, and control by TVA of hydroelectric facilities along the river which are owned by Nantahala and Tapoco. Nantahala owns hydroelectric projects upstream of Fontana Dam, while Tapoco owns projects downstream.

Nantahala and Tapoco are both wholly owned subsidiaries of Alcoa, which conducts aluminum smelting operations in Alcoa, Tennessee. Currently, Tapoco is the industrial power supply source for Alcoa's Tennessee smelting operations, while Nantahala serves a public utility load in western North Carolina. Although Tapoco (originally the Knoxville Power Company) functioned primarily to serve a public load in Tennessee until

1945, it has since 1955 devoted its output entirely to Alcoa's smelting operations. At the time of the hearing, it was not regulated by either the Tennessee Public Service Commission or the North Carolina Utilities Commission. Nantahala was created as a public utility in western North Carolina in 1929 and although it sold excess power to Alcoa until approximately 1971, sales to Alcoa then ceased due to increased demand by its public service customers. Nantahala is regulated by the North Caolina Public Utilities Commission.[1]

In 1941, Alcoa and TVA entered into the Original Fontana Agreement (OFA), a 20-year contract by which land owned by Nantahala was turned over to TVA for development of the Fontana Dam, and control of a number of Nantahala and Tapoco generating facilities was given to TVA. All of Nantahala's generation, except for three small plants, was included. In exchange, TVA agreed to provide Alcoa with a continuous stream of 11,000 kW for the term of the contract.

In 1962, a new Fontana Agreement (NFA) was executed by Alcoa, TVA, Nantahala and Tapoco. The agreement was similar to the original one, but TVA, instead of supplying Alcoa with electricity, agreed to give to Nantahala and Tapoco average annual entitlements of 1,798,000,000 kWh. Alcoa, Nantahala and Tapoco were to agree among themselves as to allocation of the entitlements. This contract is on file with the Commission as Tapoco Rate Schedule No. 3.

To allocate the entitlements from TVA, Nantahala and Alcoa entered into a 1963 Apportionment Agreement which provided that Nantahala's monthly share of the NFA entitlements would be the larger of either its total actual generation output or one-twelfth of its annual primary energy[2] capability of 360 million

[1]A more detailed description of the history of Nantahala and Tapoco is set forth at pp. 6-8 of the Initial Decision.

[2] "Primary" energy is the amount of energy generation which is virtually assured under the most adverse generation conditions. It is a theoretical minimum annual potential generation.

kWh. The balance of the entitlements was to go to Tapoco. The agreement further provided that Alcoa would pay Nantahala $89,200 per year for allowing TVA to operate its projects. This agreement was never filed with the Commission.

The 1963 Apportionment Agreement was revised by Nantahala and Tapoco, who entered into a 1971 Apportionment Agreement (Alcoa was not a party). This agreement, still in effect, limits Nantahala's share of the TVA entitlements to 360 million kWh annually. Unlike the 1963 contract, it also limits Nantahala's demand to 54,300 kW. The $89,200 annual payment by Alcoa to Nantahala is eliminated. All remaining entitlements go to Tapoco. The agreement was not filed with the Commission until 1980.

Because Nantahala's TVA entitlements are not sufficient to serve its public service load, the utility purchases additional power from TVA at approximately 19.5 mills per kWh[3]. Tapoco sells power to Alcoa at approximately 2.4 mills per kWh.[4] Adoption of Complainants'/Intervenors' position in this proceeding would eliminate cost allocation under the above described contracts and instead would compute the wholesale cost of service by rolling in the low cost Tapoco energy with the high cost TVA purchases, resulting in a lower average cost of power.

B. *Complaint Allegations*

Highlands' complaint alleges that Alcoa, Nantahala and Tapoco have violated the Federal Power Act by diverting for the benefit and private use of Alcoa hydroelectric power and facilities dedicated to public service. It claims the diversion has been accomplished by the following practices:

[3]Nantahala 1975 Form 1, p. 423, col. q. The cost of this power is passed on to Nantahala's customers through a purchased power adjustment clause, also at issue in this proceeding.

[4]Tapoco 1975 Form 1, p. 414, col. f.

(1) Alcoa has assigned the best hydroelectric generating facilities dedicated to the public service in the region to its own service through Tapoco and Tapoco's predecessor companies, leaving Nantahala to serve the public load with facilities which are claimed by Nantahala to be currently inadequate.

(2) Alcoa has caused Nantahala to relinquish assets and contractual obligations for the benefit of Alcoa without consideration.

(3) Alcoa has caused Nantahala to pool its generating resources pursuant to the terms of the NFA, but Nantahala is denied a reasonable share of the benefits of coordinated operations as power is divided between Tapoco and Nantahala.

Highlands contends that because Nantahala and Tapoco have commingled their assets and liabilities under the NFA, it is not possible to derive a rational method of apportioning costs and benefits on any basis other than a rolled-in cost of service. The town asks the Commission to pierce the corporate veil between the two utilities and treat them as one entity for ratemaking purposes, to set aside the 1971 Apportionment Agreement, to develop Nantahala's rates on a rolled-in cost of service basis, and to order Alcoa and Tapoco to establish an interconnection with Highlands. If rolled-in costing is not adopted, Highlands believes the Commission should set aside all purchased power expense claimed by Nantahala resulting from the misallocation of power received from TVA as consideration for the NFA.

C. *Discussion*

The presiding judge concluded that Highlands has not sustained its burden of proof on the issue of piercing the corporate veil and combining Nantahala and Tapoco for ratemaking purposes. However, he determined that allocation under the 1971 Apportionment Agreement is unfair. Although he refused to reform the contract, he concluded that rates should be set as if the

1971 Agreement allocated the NFA entitlements as proposed by the Commission staff. This allocation would give Nantahala that portion of the NFA entitlements which is proportionate to Nantahala's contribution of the power turned over to TVA.[5] The judge also determined that the 1971 Agreement is a contract affecting rates and charges under §205(c) of the Federal Power Act and should have been filed when made, but that Nantahala's failure to timely file does not give rise to any sanctions assessable by an administrative law judge.

Complainants/Intervenors except to the judge's decision not to require a rolled-in cost of service and the filing of joint rate schedules by Nantahala and Tapoco, the failure to recommend sanctions for the failure to file timely rate schedules, and the failure to recommend reformation of the 1971 Apportionment Agreement. The Commission staff also objects to the lack of sanctions for failure to file jurisdictional rate schedules. Nantahala excepts to the judge's adjustment of entitlements under the New Fontana Agreement.

There appears to be considerable confusion in this proceeding as to the relationship between burden of proof and establishment of a *prima facie* case. As the judge properly points out, the burden of proof in a §206 complaint proceeding is on the complainant.[6] The burden consists of coming forward with a *prima facie* case and once this initial burden is met, the burden shifts to the respondent to make an affirmative defense.[7] The judge does not distinguish the test for ultimate burden of proof from that of establishing a *prima facie* case. The test for *prima facie* evidence is whether there are facts in evidence which if unanswered would

[5]Tr. 3316-17.

[6]Section 556(d) of the Administrative Procedure Act controls allocation of burden of proof in a §206 proceeding, and places the burden on "the proponent of a rule or order . . .".

[7]*Public Service Company of New Hampshire*, Opinion No. 37, Docket No. ER76-285 (March 30, 1979 [6 FERC ¶—]) mimeo at 5.

justify men of ordinary reason and fairness in affirming the question which the plaintiff is bound to maintain.[8]

As discussed below, we do not agree that Highlands has not made a *prima facie* case as to any elements of its complaint. However, such a finding does not end the matter since it means only that the initial burden of going forward on a particular allegation of the complaint has been met. Our decision must be based on the weight of the *total* evidence, including that which the respondents present to rebut or discredit the proponent, and any available sanctions may be imposed by us according to a preponderance of the evidence.[9]

We conclude that Highlands has made a *prima facie* case to show the unfair benefits to Alcoa which have resulted from the 1971 Apportionment Agreement. However, we do not find there is substantial evidence to support a finding that the Nantahala and Tapoco systems should be treated as one, or that rolled-in costing should be adopted.

The central question to resolve here is whether a preponderance of the evidence supports a finding that Alcoa has used the separate corporate identities of Nantahala and Tapoco to frustrate the purposes of the Federal Power Act. "While corporate entities may be disregarded where they are made the implement for avoiding a clear legislative purpose, they will not be disregarded where those in control have deliberately adopted the corporate form in order to secure its advantages and where no violence to the legislative purpose is done by treating the corporate entity as a separate legal person."[10] Where a statutory purpose can be easily frustrated through the use of separate corporate entities, a regulatory commission may look through the corporate form and

[8]9 *Wigmore on Evidence* §2494, at 387 (3d ed. 1981) (citations omitted).

[9]*Steadman v. S.E.C.*, 49 U.S.L.W. 4174 (February 25, 1981).

[10]*Schenley Distillers Corp. v. U.S.*, 326 U.S. 432, 437 (1946).

treat the separate entities as one and the same for ratemaking purposes.[11]

Based on the evidence presented, we cannot find that Alcoa has used the separate corporate identities of Nantahala and Tapoco to frustrate the purposes of the Federal Power Act, or that the two companies operate as an integrated system. Nantahala and Tapoco were developed in different states and for different purposes;[12] their customer loads and sources of generation are geographically separate;[13] their management is separate;[14] and they are interconnected at only one point.[15] The two companies do not constitute an integral unit between themselves but are each a part of the coordinated TVA system, and it is TVA who controls and dispatches most of the generation from their respective generating plants.

Complainants/Intevenors cite to Commission Opinion No. 711 (*Georgia Power Co.*, 52 FPC 1343 (1974)) in support of their argument that Nantahala and Tapoco constitute an integrated system whose costs should be allocated on a rolled-in basis. Although the Commission rejected rolled-in costing in *Georgia Power,*[16] Complainants/Intervenors claim the case holds that rolled-in

[11]*General Telephone Co. of the Southwest v. U.S.*, 449 F.2d 846, 855 (5th Cir. 1971).

[12]Tr. 2373-2376; Tr. 1382-1384; Exhs. N-33 and N-34; Tr. 2634-2635.

[13]*Id.* All but one of Nantahala's plants are above the Fontana Dam Project, while Tapoco's are below. Although both companies turn over all of their output to TVA, Nantahala serves only customers in North Carolina, while all of Tapoco's customer load is in Tennessee.

[14]Exhs. S-14 and S-15; Tr. 2647; Tr. 2438-39.

[15]Exh. C/I-50. The companies are integrated through a single 161 kV line. Tr. 2383.

[16]In *Georgia Power*, the Commission rejected an argument that the costs of Georgia Power Company and Alabama Power Company, both part of the integrated Southern System Power Pool, should be allocated on a systemwide basis. Such allocation would have reduced Georgia Power's wholesale rates at the expense of Alabama Power, which had a relatively large low-cost hydroelectric capacity.

costing is appropriate where: (1) a complaining customer can show that the individual company approach is theoretically unsound because it fails to identify appropriate customer loads; (2) regardless of theory, it can be shown that customer cost responsibility is distorted by unreasonable power pool transactions. They claim they have met both of these criteria.

The record developed here does not support Complainants'/Intervenors' analysis of *Georgia Power* as applied to the unique facts of this case. As stated in *Georgia Power,* rates should be based upon costs related to the services rendered.[17] Nantahala and Tapoco serve separate customer loads and, unlike the companies in the Southern System, they do not exchange energy with each other. Any energy exchanges which take place are with TVA. Furthermore, as admitted by Complainants' witness on cross-examination, the fact that companies may be interconnected or have common dispatching does not necessarily require a finding that they constitute an integrated system or that rolled-in costing is appropriate.[18] Another of Complainants' witnesses admitted on cross-examination that Nantahala and Tapoco do not actually fit the definition of "System, Electric" which appears in the Edison Electric Institute's Glossary of Electric Utility Terms.[19]

Complainants/Intervenors allege that Tapoco is a utility dedicated to public service in western North Carolina and that it used eminent domain powers to acquire sites for certain hydroelectric projects. They argue that Nantahala was a spin-off of

[17]52 FPC at 1349.

[18]Tr. 2083-2101. For example, the Southern System Companies exchange power with one another, have common dispatching, have interconnected transmission and coordinate plant additions, yet rolled-in costing has been rejected for them. Tr. 2090-2097.

[19]Tr. 2309-2310. This definition reads: "The physically connected generation, transmission, distribution, and other facilities operated as an integral unit under one control, management, or operating supervision." The witness had earlier stated his belief that the combined Nantahala and Tapoco facilities met this definition. Tr. 1979.

the former Tallahassee Power Company (a public service corporation whose name was later changed to Carolina Power Company), and that Tallahassee's assets in western North Carolina were later spun off to Tapoco in 1955. The evidence shows that in 1934 Tallahassee Power condemned one acre of land for the Santeetlah Project reservoir, which is now owned by Tapoco.[20] It has not been shown that Tapoco has condemned any land. We do not find this evidence or the fact that Nantahala and Tapoco acquired Tallahassee Power Company assets some 25 years apart supports a finding that the two companies should be treated as one, or that the Respondents have abused the Federal Power Act.[21]

It is next necessary to examine any intercorporate transactions between Nantahala and Tapoco which might distort customer cost responsibility. The pertinent transactions here are the Old and New Fontana Agreements and subsequent apportionment agreements, particularly the 1971 Apportionment Agreement. Upon review of these contracts, we agree with the presiding judge that the 1971 Agreement is unfair, but we cannot accept Complainants' contention that Alcoa, through the OFA or NFA, intentionally deprived Nantahala of adequate hydroelectric generating facilities to serve its public load.

The record shows that the 1941 OFA and 1962 NFA were the result of arms' length bargaining. The OFA was negotiated at a time when a rapid increase in electricity was necessary to supply the aluminum smelting facilities at Alcoa, Tennessee, for the war effort.[22] Prior to this time Nantahala primarily had served its small public service load in North Carolina. Nantahala's public service

[20]Tr. 2374; Exh. C/I-45.

[21]We note that subsequent to the hearings and briefing of this case, but prior to the initial decision, the North Carolina Utilities Commission issued a decision finding that Tapoco is a public utility under North Carolina law. However, the definition of "public utility" in North Carolina is peculiar to that state and not determinative of the issues to be decided here.

[22]Tr. 1383.

load was not great enough to support additional hydroelectric projects, but because of national defense needs, Nantahala accelerated development of its Nantahala and Thorpe projects to help supply more power to Alcoa.[23] Nantahala also contemplated developing the Fontana site but did not do so because the size of its load did not justify developing such a large project, TVA had Congressional authority to develop the site, and TVA could do so much faster than could Nantahala.[24] It was under this historical setting that Alcoa, as parent of Nantahala, entered into the OFA. Nantahala transferred to TVA its property rights in the Fontana area for approximately $1.9 million and gave control to TVA of a number of its generating facilities, including the Thorpe and Nantahala projects then under construction.[25] In exchange, Nantahala received the energy the Nantahala and Thorpe projects would generate, which was far in excess of the demands of its then existing North Carolina load.[26]

By the late 1950's, when the OFA was about to expire, Nantahala found it necessary to supply itself with a more firm power supply since its public load had grown from 3 MW in the 1930's to approximately 41.3 MW in 1962.[27] Firmer supply was also necessary for Alcoa, which was contemplating expansion at its Alcoa, Tennessee, operations.[28] At about the same time that negotiations for the NFA began, Nantahala sought to sell its distribution system to Duke Power Company in order to provide inexpensive and more reliable power to its customers.[29] Although this proposed transfer to Duke was being pursued and although Nantahala did not directly participate in the NFA negotiations, the record indicates the negotiators considered the possibility that the sale

[23]Tr. 1383; Tr. 2375.

[24]Tr. 1383-84.

[25]Tr. 1384; Exh. N-37.

[26]Tr. 1384.

[27]Tr. 2378.

[28]*Id.*

[29]Tr. 1386; Tr. 2680. The sale to Duke was approved by the North Carolina Utilities Commission and North Carolina Court of Appeals, but rejected by the North Carolina Supreme Court.

would not occur and that Nantahala's needs might have to be met in the NFA.[30]

The above history of the OFA and NFA indicates no intent on the part of any of the parties to ignore the needs of Nantahala's public service customers or deprive them of energy at just and reasonable rates.

The apportionment agreements are another matter. The 1963 Agreement between Alcoa and Nantahala was entered at a time when Nantahala had excess energy which it sold to Alcoa. By 1971, however, Nantahala not only had no excess energy to sell to Alcoa, but it also did not have sufficient energy to meet its public load requirements. The utility investigated the possibility of withdrawing from the NFA and negotiating directly with TVA for a firm energy and demand supply in exchange for the use of Nantahala's plants, as well as contracting for additional firm power necessary to meet its growing public load.[31] TVA informed Nantahala that even if Nantahala could withdraw from the NFA, TVA could not be expected to provide the company with any greater portion of firm power than is supplied proportionately under the NFA.[32] Nantahala then negotiated the 1971 Apportionment Agreement with Tapoco, so that it could reach an agreement on its Fontana entitlements before setting final arrangements with TVA for purchasing additional power.[33] Such an agreement was necessary because a significant portion of the total power entitlements received under the NFA were curtailable or interruptible, and Nantahala had to make sure it would receive firm capacity and energy necessary for a public load.[34]

The alleged fairness of the 1971 Agreement is not supported by the record. The 1963 Agreement gave Nantahala considerably

[30]Exhs. T-34 at 15, T-61 through T-67(A), and C/I-106 at 5.

[31]Exh. N-43.

[32]Id.

[33]Tr. 1389.

[34]Tr. 1390.

greater benefits than does the 1971 Agreement, and there is no indication in the record as to why Nantahala, without consideration, gave up those benefits. The 1963 Agreement gave Nantahala energy entitlements equal to the *greater* of: (1) its actual generation for the month *or* (2) $^1/_{12}$ of its annual primary generating capability of 360 million kWh. The 1971 Agreement limits Nantahala to 360 million kWh per year. Thus, in periods of favorable rainfall and stream flow, Nantahala's customers may have to pay for extra energy purchased from TVA even though Nantahala's facilities actually generate more energy than the customers require. Unlike the 1963 Agreement, which contained no capacity limitation for Nantahala, the 1971 Agreement also limits Nantahala's demand to 54,300 kW. The 1963 Agreement provided that Alcoa would pay $89,200 annually to Nantahala as compensation for allowing TVA to operate Nantahala's facilities. The record gives no explanation as to why these payments were dropped in 1971.

The 1963 Apportionment Agreement was to continue in effect during the term of the 1962 NFA, which was 20 years.[35] We cannot find the 1971 Agreement fairly represents the interests of Nantahala's customers since there is not sufficient evidence to show that Nantahala received any consideration for entering into the less favorable contract after approximately eight years under the NFA. As pointed out in the initial decision, the only explanation offered by Respondents was that a 1963 North Carolina Utilities Commission decision rendered the 1963 contract moot. The record does not bear this out since the NCUC orders themselves modified only Nantahala's retail sales arrangement, and did not even mention the apportionment contract.[36] Also, the staff witness testified that the parties continued to operate under the agreement until 1971, that Alcoa and Nantahala entered a July

[35] Exh. C/I-84 at 3.

[36] Docket No. E-13, Sub. 13. See Items 2 and 3 of July 14, 1978 Appendix to Town of Highlands brief in opposition to Nantahala's motion to sever.

31, 1971 contract which specifically terminated the 1963 Agreement, and that Nantahala's Forms No. 1 for the years 1963 through 1971 show a continuation of the $89,200 compensation payments.[37]

We agree with the judge and staff that the most equitable division of entitlements would give Nantahala that portion of the NFA entitlements which is proportionate to the utility's actual contribution of power turned over to TVA. Staff Exhibit 7 shows the actual net generation of the Nantahala and Tapoco facilities for the years 1963-1978. The total net generation for Nantahala for 1963-1969, the pertinent time period here, was 22.50 percent of the total combined net generation of the two companies for the same years. The appropriate energy entitlement for Nantahala therefore would be 404,268,300 kWh (22.50 percent of the total 1.8 billion kWh entitlements from TVA).[38] The appropriate capacity credit would be 54.3 MW.[39]

The 404,268,300 energy entitlement was derived as follows:

Total Average Energy Available (Normal Year)	1,796,748,000 kWh
Primary Energy (Normal Year)	1,071,014,667 kWh
times Entitlement Percentage	22.50
Nantahala's Primary Energy Entitlement	240,978,300 kWh
Secondary Energy (Normal Year) [1,796,748,000 Less 1,071,014,667]	725,733,333
times Entitlement Percentage	22.50
Nantahala's Secondary Energy Entitlement	163,290,000 kWh
Total Nantahala Energy Entitlement	404,268,300 kWh

[37] Tr. 3312-13.

[38] Tr. 3325.

[39] Exh. T-33; Tr. 2675-76. At Tr. 3318 the staff states that the amount of capacity from TVA under the Apportionment is equitable.

We note that the 404,268,300 figure represents an entitlement for the "average" year, not the test year amount. The average entitlement provides a reasonable and consistent amount of energy to Nantahala each year, and is not susceptible to variation in water flows as witnessed between the average and test year amounts. Also, the average is more consistent with the operations of hydroelectric systems and the time frame of the 1971 Agreement. We therefore conclude that Nantahala should use the "average" entitlement in developing its costs.

Our decision here does not reform the 1971 Agreement, and does not affect the elimination of the $89,200 annual compensation payment from Alcoa to Nantahala. The effect of this opinion is to provide entitlements to Nantahala which will result in just and reasonable rates to its wholesale customers.

To the extent that allocation of the energy entitlements pursuant to the 1971 Agreement has resulted in unnecessary energy purchases by Nantahala from TVA, we shall require Nantahala to make refunds to its customers for the locked-in period of this docket. Nantahala shall be required to refund, with interest, any amounts collected in excess of those which would have been payable by customers had Nantahala received entitlements as described in the preceding paragraphs.

D. *Filing Requirement/Sanctions*

Section 205(c) of the Federal Power Act provides:

> Under such rules and regulations as the Commission may prescribe, every public utility shall file with the Commission, within such time and in such form as the Commission may designate, . . . schedules showing all rates and charges for any transmission or sale subject to the jurisdiction of the Commission, and the classification, practices, and regulations affecting such rates and charges, *together with all contracts which in any manner affect or relate to such rates, charges, classifications, and services.* [Emphasis added.]

The Commission staff claims the presiding judge properly held that the 1971 Apportionment Agreement is a contract affecting rates and charges under Section 205(c), but that the judge erred in failing to recommend civil sanctions against Nantahala and Tapoco under Section 315(a), for failing to timely file the 1963 and 1971 Apportionment Agreements. Complainants/Intervenors argue that the fairest sanction is to treat Nantahala and Tapoco as one company and adopt rolled-in costing. If this is not done, they assert that the case should be referred to the Justice Department for criminal prosecution.

The Commission agrees with the law judge that the Apportionment Agreements clearly are contracts affecting, in some manner, rates and charges under Section 205(c) of the Federal Power Act, and should have been filed when made. However, civil sanctions under Section 315(a) of the Act are not available. Section 315(a) provides:

> "Any licensee or public utility which willfully fails, within the time prescribed by the Commission, to comply with any order of the Commission, to file any report required under this Act or any rule or regulation of the Commission thereunder, to submit any information or document required by the Commission in the course of an investigation conducted under this Act, . . . shall forfeit to the United States an amount not exceeding $1,000 to be fixed by the Commission after notice and opportunity for hearing."

The Commission never issued an order to Nantahala or Tapoco to file either of the Agreements as rate schedules, the Agreements are not reports required under the Act or regulations, and are not documents required by the Commission in the course of an investigation.[40] We therefore conclude that sanctions are not appropriate.

[40] The evidence on which the staff and Complainants/Intervenors rely consists of a series of letters between Nantahala and the Commission between 1963 and 1968 (Exhs. C/I-89-92). The letters show that Nan-

(*Footnote continued on following page*)

* * *

Motion to Notice Facts

Nantahala filed a motion on July 13, 1981, requesting that the Commission take official notice of statistics which show Nantahala's actual generation in kWh and New Fontana entitlements for June 1980 through May 1981. The figures purportedly represent Nantahala's generation and entitlements under drought conditions, and state the total 12 months' generation net of losses as 268,488,000 kWh and the total entitlements as 360,036,000 kWh. Both the Complainants/Intervenors and Commission staff oppose the motion.

Nantahala's motion is denied. The company claims the proffered statistics completely refute the Commission staff witness' testimony, but it gives no source of the statistics and offers no explanation as to why Nantahala's generation under drought conditions during a one-year period should influence our analysis of the fairness of the 1971 Apportionment Agreement. The data does not include capacity figures for Nantahala, and provides neither capacity nor energy statistics for Tapoco during 1981. Also, the figures reflect TVA's operating control over Nantahala's reservoirs, rather than what Nantahala's generation would be were it dispatching its own generation to best meet its own load requirements.

The staff apportionment study, upon which we relied herein, was based on seven years of actual stream flows for Nantahala,

(*Footnote continued from preceding page*)
tahala filed *under protest* a certificate of concurrence in Tapoco's filing of the New Fontana Agreement as a rate schedule. The Secretary of the Commission accepted the certificate of concurrence and noted that the Alcoa-Nantahala reimbursement agreement should also be filed as a rate schedule. The company responded that it did not believe Nantahala's power sales arrangements with Alcoa are subject to Commission jurisdiction. This evidence does not prove that any sanctions should be imposed or any other actions should be taken by the Commission with respect to Section 315 or 316 of the Federal Power Act.

and was taken from Forms No. 1 filed by the company. The information here reflects only one year of data and does not indicate how the statistics were compiled. The figures used by staff, for the years 1963–1969, were the same ones available to the companies at the time the 1971 Agreement was negotiated. We believe those figures are a far more reliable means of evaluating the reasonableness of the agreement at the time it was made. Statistics based on an isolated year some ten years after the agreement was made are of no substantial value in determining the fairness of the apportionment.

* * *

The Commission orders:

(A) The initial decision issued in this proceeding on April 10, 1981, is affirmed to the extent not modified herein.

(B) Within 75 days of the issuance of this order, Nantahala shall file revised rate schedules and tariff sheets in accordance with the findings and conclusions herein.

(C) Within 30 days of the Commission's approval of the revised tariff sheets, Nantahala shall refund to its customers, with interest, any amounts collected which are in excess of those allowed herein.

(D) Within 30 days of making refunds, Nantahala shall file with the Commission, in writing and under oath, a report showing the amount of refunds made, the method of computation used, together with releases from its jurisdictional customers.

(E) Any exceptions to the initial decision not granted herein are denied.

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APPENDIX J

Excerpts From FERC Opinion No. 139-A,
Nantahala Power and Light Company,
Docket Nos. ER76-828-002,-003,-004,-005;
Town of Highlands, North Carolina
v. Nantahala Power and Light Company,
Docket Nos. EL78-18-002,-003,-004,-005

Nantahala Power and Light Company, Docket Nos. ER76-828-002, -003, -004, -005;

Town of Highlands, North Carolina, *et al.* v. Nantahala Power and Light Company, Docket Nos. EL78-18-002, -003, -004, -005

Opinion No. 139-A, Order Denying Rehearing

(Issued September 30, 1982)

Before Commissioners: C. M. Butler III, Chairman; Georgiana Sheldon, J. David Hughes, A. G. Sousa and Oliver G. Richard III.

On May 14, 1982, the Commission issued Opinion No. 139, an opinion and order modifying the initial decision issued in this proceeding on April 10, 1981. Applications for rehearing of Opinion No. 139 were filed by the Town of Highlands, North Carolina, *et al.* (Highlands), the Attorney General of the State of North Carolina, Nantahala Power and Light Company (Nantahala), Aluminum Company of America (Alcoa), and Tapoco, Inc. Highlands also filed a motion to lodge a June 8, 1982 order of the North Carolina Utilities Commission (NCUC) which deals with a recent Nantahala retail rate case before that Commission.

By order issued July 9 [20 FERC ¶ 61,026], the Commission granted rehearing for the sole purpose of further consideration, stayed the effect of Opinion No. 139 pending the issuance of an order on the merits of the issues raised on rehearing, and gave notice of its intent to act on Highlands' motion to lodge. This order addresses the merits of the various filings. Because many of the arguments raised on rehearing are repetitious and were already considered fully by the Commission, we will address only those matters which warrant further discussion.

Burden of Proof

Highlands and the Attorney General make three basic arguments on rehearing concerning the burden of proof in this con-

solidated proceeding: (1) the Commission erred in assigning the initial burden of proof to Complainants and in finding that Nantahala had carried its burden to justify its proposed rates and charges; (2) the Commission explicitly imposed the ultimate burden of proof on Complainants; (3) to the extent the Commission indicated that Complainants did not make a *prima facie* case as to all elements of their complaint, this conflicts with Judge McGowan's February 28, 1979 procedural order which preceded the actual hearing of the case.

Contrary to allegations of the Attorney General, the Commission did not conclude that the issues concerning the intercorporate relationships among Alcoa, Nantahala and Tapoco were raised exclusively in the complaint docket. Page 2 of Opinion No. 139 recognizes that the issues of corporate misuse were raised in both the complaint and the rate docket. The Commission properly placed the burden of proof in the complaint docket on the Complainants and the burden of proof in the rate increase docket on Nantahala.

As to the numerous arguments concerning whether or not Complainants established a *prima facie* case as to every element of their complaint, these arguments obscure the real question before us, that is, whether the *totality* of the evidence presented supports a finding that rolled-in costing should be adopted. As indicated on page 6 of our Opinion, the criterion for deciding the issues here is substantial evidence. Although the Complainants in a proceeding may establish a *prima facie* case as to their allegations, that satisfies only the initial burden of going forward with their burden of proof. The Commission must consider not only the *prima facie* evidence, but also all evidence to rebut or discredit the *prima facie* case. Our decision in both the complaint and the rate increase proceedings rests on a weighing of all the evidence presented.

Highlands and the Attorney General cite to Judge McGowan's February 28, 1979 pretrial order in which the judge stated, at pages 9-10:

> Nantahala, Alcoa and Tapoco have attempted to rebut the *prima facie* case of corporate misuse established by Highlands . . . a factual question remains as to whether or not Nantahala receives the proper benefit of its own capacity, energy, and storage contributions. This question cannot be resolved by summary disposition and must therefore be set for hearing.

Judge McGowan went on to pierce the corporate veil between Alcoa and Tapoco for the limited purpose of making Alcoa a party. What Highlands and the Attorney General neglect to observe in their arguments is that the judge expressly stated at page 15 of his order that he was treating Alcoa and Tapoco as one for limited procedural purposes and that he was in no way passing on the merits of Highlands' allegations. He further stated:

> . . . In addressing the merits of Highlands' allegations, Highlands may yet attempt to show that the Commission should further pierce the corporate veil which allegedly surrounds Alcoa, Tapoco and Nantahala so that these three companies may be treated as one for relief purposes. I intend no ruling on the substance of Highlands' other allegations at this time.

Opinion No. 139 in no way conflicts with Judge McGowan's procedural order. Furthermore, a finding that the 1971 Apportionment Agreement is unfair does not mandate a finding that the Nantahala and Tapoco systems should be treated as one for ratemaking purposes.

We recognize that the North Carolina Utilities Commission (NCUC), based on a similar record, reached a different conclusion concerning rolled-in costing. However, the question of whether to treat various entities as an integrated system for ratemaking purposes is not a purely factual question, but also rests on criteria which each ratemaking authority may deem relevant. The Attorney General argues that the Commission erred by giving controlling weight to the corporate separateness of Nantahala

and Tapoco, and affording this separate status a significance not afforded under North Carolina law. As discussed below, it is not true that our Opinion gave controlling weight to this factor, or any other.

Highlands and the Attorney General argue that the Commission gave improper weight to various factors such as corporate separateness, separation of management, and geographic separation of customer loads. We wish to emphasize that no one factor was decisive in our decision not to adopt rolled-in costing. Rather, our decision rests on a variety of factors mentioned in both the initial decision and at page 7 of our Opinion.

The Attorney General contends that the Commission improperly established as an element of Complainants' case the necessity of proving that Alcoa used the separate corporate indentities of Nantahala and Tapoco to frustrate the purposes of the Federal Power Act. However, as pointed out in Judge McGowan's February 28, 1979, pretrial order, Complainants themselves cited numerous cases for the proposition that the corporate veil may be pierced where separate corporate indentities have been used to avoid a clear legislative purpose. The Commission did not introduce any new element of proof for Complainants. Nor, as the Attorney General claims, did we introduce an element of intent by Alcoa to deprive customers of just and reasonable rates. Although we did look at Alcoa's intent during the formation of the companies and negotiations of the agreements at issue here, that was not determinative of the issue of whether separate corporate identities have been used to frustrate the purposes of the Federal Power Act.

The Attorney General next claims that Opinion No. 139 fails to address the effect the Fontana agreements have had on Nantahala's ability to render service at just and reasonable rates, and that the Commission ignored certain benefits Alcoa received under the agreements to the detriment of Nantahala. Specifically,

he points to the benefits Tapoco (and thereby Alcoa) receives from the storage contributions of Nantahala's upstream projects. TVA, through the Fontana Dam which is downstream of Nantahala, benefits from Nantahala's upstream storage. Tapoco, which is downstream from the Fontana Dam, in turn receives downstream benefits from TVA. Although Tapoco indirectly receives downstream benefits from Nantahala, the Attorney General ignores other trade-offs in the agreements such as the $89,000 per year compensation payment to Nantahala. Furthermore, the extent of any downstream benefits has not been shown in the record.

In reference to the Attorney General's contention that Opinion No. 139 does not enunciate and apply ascertainable standards relating to the statutory requirement that rates be non-discriminatory, he ignores the evidence which shows that there is a difference in the quality of service received. Although there is a price discrepancy in the rates paid by Nantahala and Tapoco, Nantahala receives all of the primary energy available under the NFA, and a majority of the firm capacity.[1] Tapoco receives the remaining curtailable and interruptible capacity and energy. The firm capacity available to Nantahala is capacity which is available 100 percent of the time and not subject to unit outages. The Commission staff, who originally advocated 68.3 MW of capacity for Nantahala, later retreated from this position and concluded that if the NFA structure were taken as given, the 54.3 MW of capacity to Nantahala is fair.[2] Given the type of capacity and Nantahala's capacity contributions, we agree.

[1]Exhs. T-32 and T-33. Nantahala receives 54.3 MW firm capacity. Its installed nameplate capacity is 97.2 MW. Tapoco receives 13 MW firm, 75 MW interruptible and 90 MW curtailable capacity. Tapoco's installed nameplate capacity is 326.5 MW.

[2]Tr. 3318. The presiding judge, in approving the staff's position, apparently mis-read the staff's final position concerning appropriate capacity entitlements. See Staff Brief Opposing Exceptions. Opinion No. 139 modified the initial decision to this extent.

Exclusion of Evidence

The Commission summarily affirmed the initial decision's exclusion of several exhibits by which Complainants/Intervenors sought to prove that the former owner of two Tapoco projects (Tallahassee Power Company) had the power to condemn the land on which those projects were built. These exhibits are C/I 39(a) to 39(d), C/I 40(a) to 40(h) and C/I 41(a) to 41(f). Highlands and the Attorney General object to our summary affirmance.

Highlands maintains in this proceeding that Tallahassee was a predecessor to Tapoco and Nantahala, and attempts to show through the disputed evidence that Tallahassee deliberately held itself out as a public utility having the right of eminent domain. Tallahassee's charter from the North Carolina legislature did grant the company eminent domain power. However, none of the excluded exhibits prove that the Tapoco facilities were dedicated to public service. Furthermore, all of the cases to which the exhibits relate represent claims which were settled and never went to trial, and are not relevant evidence to establish Highlands' claim that costs should be rolled-in.

Modification of Entitlements

Alcoa and Nantahala claim that Opinion No. 139 may result in confiscation of property by setting rates below Nantahala's actual costs. The order sets rates as though a portion of interruptible entitlements were allocated to Nantahala. Both parties contend that proper rates must reflect the cost of firming up the interruptible energy in order to make it usable to Nantahala. According to a study presented by Nantahala on rehearing, the cost of firming up the secondary energy would be $489,147 in the test year and $1.2 million at current costs. Nantahala claims the Commission, at a minimum, should grant rehearing so that it can consider whether the cost of firming up the secondary power attributed to Nantahala outweighs the benefit of such energy.

We deny rehearing on this issue. Nantahala's study of the costs associated with firming up the interruptible energy entitlements is extra-record evidence which was not subjected to cross-examination by any other parties. Nantahala had ample opportunity to submit such a study prior to the close of the record. It did not.

In determining just and reasonable rates in Opinion No. 139, the Commission did not choose to reform the 1971 Apportionment Agreement and was not concerned with the mechanics of how entitlements of energy from TVA are allocated to each party, as long as each party receives its fair share of energy based on that party's contribution of actual energy turned over to TVA. The mechanics of the proportions of both primary and secondary energy available from TVA rests with the parties. Our concern is that each party receive its proper entitlement. Nantahala entered into a 1971 contract which we find unfair. As a result, the company had to make purchases from TVA which otherwise would not have had to be made. Nantahala must bear the consequences of its acts and refund rates collected to recover the cost of the excess purchases.

* * *

Effect on Tapoco

Tapoco, Inc. has filed a statement of understanding or, in the alternative, an application for rehearing. The company states its understanding that Opinion No. 139 in no way modifies its jurisdictional power sales arrangements under its Rate Schedule Nos. 3 and 4. Under Rate Schedule No. 3, Tapoco receives capacity and energy entitlements from TVA in exchange for the output of its licensed hydroelectric project. Under Rate Schedule No. 4, it sells capacity and energy to Alcoa.

Tapoco's understanding is correct. As found by the presiding judge, no showing was made on this record that Tapoco has unjustly benefitted under these rate schedules. Accordingly, Tapoco's jurisdictional sales arrangements remain unaffected.

Effective Date of Rates

Highlands and the Attorney General of the State of North Carolina contend that the Commission's modification of Nantahala's entitlements can be prospective only, that it constitutes retroactive ratemaking, and is in violation of the filed rate doctrine. At the time of Nantahala's rate filing, the NFA was the only wholesale rate schedule in effect which governs interstate power supply coordination and sets compensation rights for Nantahala's dedication of resources to TVA. (The Apportionment Agreement was not filed until 1980.) Although the parties' arguments are somewhat unclear, their final contention is that because compensation from TVA to Nantahala and Tapoco is commingled under the NFA, the rates must be set on a rolled-in basis.

Alcoa and Nantahala also argue that the Commission's Opinion improperly modifies the NFA and Apportionment Agreement by retroactively imposing a different apportionment to Nantahala. Their arguments also are rather murky, and they cite to cases which address the filed rate doctrine to support their contention that changes in Nantahala's rate must be prospective only. Nantahala further cites *Public Service Commission of New York* v. *F.E.R.C.*, 642 F.2d 1335 (D.C. Cir. 1980), *cert. denied*, 102 S. Ct. 360 (1981) (hereinafter *Transco*), for the proposition that the company's burden of justifying its rate increase does not extend to portions of the filing it does not seek to change, specifically the allocation of entitlements.

The parties apparently misconstrue the filed rate doctrine and the prohibition against retroactive ratemaking. Neither concept has been violated by Opinion No. 139. Docket No. ER76-828 originated with a proposed rate increase by Nantahala under its Rate Schedule PL, which governs charges to customers using electric service for resale. That proposed rate increase was set for hearing under both Sections 205 and 206 of the Federal Power Act, thus giving the Commission authority to order refunds

should it find Nantahala's rates were not just and reasonable. In Opinion No. 139 the Commission found the proposed charges were not just and reasonable. Among the reasons for our finding was that the 1971 Apportionment Agreement, which is an amendment to the NFA (Nantahala's Rate Schedule No. 1), does not afford Nantahala its fair share of NFA energy entitlements, and the rates under Rate Schedule PL are directly affected by the amount of entitlements received by Nantahala. The Commission specifically stated that it was not reforming the 1971 Apportionment Agreement. Instead, the Opinion sets rates for Nantahala as though it had received its fair share of entitlements. The Commission properly acted under Section 205 of the Federal Power Act in setting just and reasonable rates.

The rule against retroactive ratemaking is that a utility may not set rates to recoup past losses, nor may a Commission prescribe rates on that principle.[3] Utility refunds for past excessive rates are thus barred, as is the Commission's retroactive substitution of an unreasonably high or low rate with a just and reasonable rate.[4] There has been no retroactive substitution of rates in Docket No. ER76-828. By order issued August 31, 1976, 56 FPC 2937, we suspended Nantahala's rates in that docket until October 1, 1976. Opinion No. 139 does not affect rates prior to that date. It deals only with the time period covered by the revised Rate Schedule PL.

The filed rate doctrine is equally clear. A company can claim no rate as a legal right that is other than the filed rate, whether fixed or merely accepted by the Commission.[5] The considerations underlying the doctrine "are preservation of the

[3]*Nader* v *F.C.C.*, 520 F.2d 182, 202 (D.C. Cir. 1975); *City of Piqua* v. *F.E.R.C., 610 F.2d 950, 954 (D.C. Cir. 1979); Public Service Co. of N.H.* v. *F.E.R.C., 600 F.2d 944, 957 (D.C. Cir. 1979).*

[4]*City of Piqua, supra; Public Service Co. of N.H., supra.*

[5]*Montana-Dakota Utilities Co.* v. *Northwestern Public Service Co.*, 341 U.S. 246, 251 (1951).

agency's primary jurisdiction over reasonableness of rates and the need to insure that regulated companies charge only those rates of which the agency has been made cognizant."[6] Nantahala claims no more than the filed rate in Docket No. ER76-828, and Opinion No. 139 gives Nantahala no more than the filed rate. The Opinion determines that the filed rate does not constitute a just and reasonable rate.

The Commission, in acting within its powers under Section 205 of the Federal Power Act, is not limited to setting new rates on a prospective basis only. It is true that we would be prohibited from relieving a company of an improvident contract unless we made a Section 206 finding that rates under the contract were so low as to adversely affect the public interest.[7] In this case, however, we have not modified Nantahala's contracts. Instead, we have set just and reasonable rates under our powers under Section 205. As to Nantahala's citation to the *Transco* case, *supra,* that case dealt with the Commission's attempt to alter a company's historical rate design which did not affect the overall level of rates, *i.e.*, Transco was merely a stakeholder and it was the individual customer groups who would be affected by the rate design. In contrast, this case involves the prudence of the costs incurred by Nantahala. Nantahala's entire rate filing was suspended and made subject to refund under Section 205, and the company bears the burden of proving all elements of the filing which will affect overall costs and resulting rates.[8]

[6]*City of Cleveland* v. *F.P.C.*, 525 F.2d 845, 854 (D.C. Cir. 1976).

[7]*Sierra Pacific Power Co.* v. *F.P.C.*, 350 U.S. 348, 355 (1956); *Pacific Gas and Electric Co.* v. *F.P.C.*, 267 F.2d 165, 166 (D.C. Cir. 1959).

[8]*North Penn Gas Co.*, 18 FERC ¶ 61,275 (1982); *Connecticut Yankee Atomic Power Co.*, Opinion No. 102, 13 FERC ¶ 61,154 (1980). See also *Cities of Batavia* v. *F.E.R.C.*, Nos. 80-1072 and 81-1270 (D.C. Circuit February 9, 1982) at 23, in which the court stated that it does not read the *Transco* decision "as precluding the Commission from reviewing a revised rate completely to assure that all of its parts—old and new—operate in tandem to insure a 'just and reasonable' result . . ."

One further point should be made. Absent compelling reasons to the contrary, we think it inappropriate to require refunds which would bring the company's rate below the superseded rate. No such compelling reasons have been shown here. We therefore conclude that the total refunds ordered herein shall not exceed the difference between the amounts that would have been collected under the superseded rate schedules and the amounts that were collected pursuant to the rate schedules at issue herein. In other words, the superseded rate shall act as a floor for refund purposes. Otherwise, the compliance rates shall be consistent with Opinion No. 139.

* * *

The Commission orders:

(A) The applications for rehearing of Opinion No. 139, filed June 11 and June 14, 1982 in the above dockets, are denied.

(B) The stay of the effectiveness of Opinion No. 139, granted by our order issued July 9, 1982, is hereby lifted. Nantahala shall make appropriate refunds with interest, in accordance with the terms of our opinions in these dockets.

APPENDIX K

Notices Of Appeal

No. 227A83 TENTH DISTRICT

SUPREME COURT OF NORTH CAROLINA

STATE OF NORTH CAROLINA, ex rel. Utilities Commission; RUFUS L. EDMISTEN, ATTORNEY GENERAL; PUBLIC STAFF, HENRY J. TRUETT; CHEROKEE, GRAHAM and JACKSON COUNTIES; TOWNS OF ANDREWS, BRYSON CITY, DILLSBORO, ROBBINSVILLE, and SYLVA; and THE TRIBAL COUNCIL OF THE EASTERN BAND OF CHEROKEE INDIANS, Appellees, v. NANTAHALA POWER AND LIGHT COMPANY; ALUMINUM COMPANY OF AMERICA; and TAPOCO, INC., Appellants.	FROM THE NORTH CAROLINA SUPREME COURT CASE NO. 227A83—Utilities Decided July 3, 1985

NOTICE OF APPEAL TO THE UNITED STATES SUPREME COURT BY NANTAHALA POWER AND LIGHT COMPANY [FILED JULY 23, 1985]

TO THE HONORABLE SUPREME COURT OF THE UNITED STATES

Applicant Nantahala Power and Light Company (hereinafter Nantahala) hereby appeals to the United States Supreme Court from the judgment of the North Carolina Supreme Court in Case No. 227A83—Utilities, issued July 3, 1985, affirming the North

Carolina Utilities Commission order issued August 17, 1982 in Docket No. E-13, Sub 29 (Remanded). The judgment of the North Carolina Supreme Court affirmed the North Carolina Utilities Commission's order reducing Nantahala's retail rates and requiring Nantahala to make refunds to its retail customers.

Nantahala gives notice that it appeals from the entire above described judgment of the North Carolina Supreme Court on the ground that the North Carolina Supreme Court upheld the validity of a North Carolina statute, as that term has been interpreted under 28 U.S.C. §1257(2) and its predecessors, which statute had been challenged on the ground of its being repugnant to the Constitution and laws of the United States. Nantahala's notice of appeal is taken pursuant to 28 U.S.C. §1257(2).

NANTAHALA POWER AND LIGHT COMPANY

By____________________
Counsel

OF COUNSEL:

Edward S. Finley, Jr.
William D. Johnson
HUNTON & WILLIAMS
Post Office Box 109
Raleigh, North Carolina 27602
(919) 828-9371

No. 227A83 TENTH DISTRICT

SUPREME COURT OF NORTH CAROLINA

STATE OF NORTH CAROLINA, ex rel. Utilities Commission; RUFUS L. EDMISTEN, Attorney General; PUBLIC STAFF; HENRY J. TRUETT; CHEROKEE, GRAHAM and JACKSON COUNTIES; TOWNS OF ANDREWS, BRYSON CITY, DILLSBORO, ROBBINSVILLE and SYLVA; MURIEL MANEY; SWAIN COUNTY BOARD OF COUNTY COMMISSIONERS; DEROL CRISP; and THE TRIBAL COUNCIL OF THE EASTERN BAND OF CHEROKEE INDIANS,

Appellees,

v.

NANTAHALA POWER AND LIGHT COMPANY; ALUMINUM COMPANY OF AMERICA; and TAPOCO, INC.,

Appellants.

COURT OF APPEALS (Wake County) No. 8210UC1034

UTILITIES COMMISSION Docket No. E-13, Sub 29

NOTICE OF APPEAL TO THE SUPREME COURT OF THE UNITED STATES [FILED JULY 23, 1985]

Notice is hereby given that Aluminum Company of America appeals to the Supreme Court of the United States from the final judgment of the Supreme Court of North Carolina entered herein on July 3, 1985. This appeal is taken pursuant to 28 U.S.C. §1257(2).

Respectfully submitted this 23rd day of July, 1985.

LeBoeuf, Lamb, Leiby & MacRae

By: ____________________

Ronald D. Jones
336 Fayetteville Street
P.O. Box 750
Raleigh, North Carolina 27602
(919) 833-9789

No. 227A83 TENTH DISTRICT

SUPREME COURT OF NORTH CAROLINA

STATE OF NORTH CAROLINA, ex rel. Utilities Commission; RUFUS L. EDMISTEN, Attorney General; PUBLIC STAFF; HENRY J. TRUETT; CHEROKEE, GRAHAM and JACKSON COUNTIES; TOWNS OF ANDREWS, BRYSON CITY, DILLSBORO, ROBBINSVILLE and SYLVA; SWAIN COUNTY BOARD OF COUNTY COMMISSIONERS; DEROL CRISP; and THE TRIBAL COUNCIL OF THE EASTERN BAND OF CHEROKEE INDIANS,

Appellees,

v.

NANTAHALA POWER AND LIGHT COMPANY; ALUMINUM COMPANY OF AMERICA; and TAPOCO, INC.,

Appellants.

UTILITIES COMMISSION Docket No. E-13, Sub 29

NOTICE OF APPEAL TO THE SUPREME COURT OF THE UNITED STATES [FILED SEPTEMBER 23, 1985]

Notice is hereby given that Tapoco, Inc. appeals to the Supreme Court of the United States from the final judgment of the Supreme Court of North Carolina entered herein on July 3, 1985. This appeal is taken pursuant to 28 U.S.C. §1257(2).

Respectfully submitted this 23rd day of September, 1985.

LeBoeuf, Lamb, Leiby & MacRae

____

David R. Poe
336 Fayetteville Street
P.O. Box 750
Raleigh, North Carolina 27602
(919) 833-9789

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APPENDIX L

Opinion Of The Eighth Circuit In *Middle South Energy, Inc. v. Arkansas Public Service Commission,* Nos. 84-2409, 84-2410, and 84-2480 (filed Aug. 23, 1985)

UNITED STATES COURT OF APPEALS

FOR THE EIGHTH CIRCUIT

No. 84-2409
No. 84-2410
No. 84-2480

Middle South Energy, Inc., and Arkansas Power and Light Company,
Appellees,

v.

Arkansas Public Service Commission; Robert E. Johnston, Commissioner; Patricia S. Qualls, Commissioner; and James W. Daniel, Commissioner; Attorney General of Arkansas; and Ratepayers Fight Back,
Appellants.

Appeal from the United States District Court for the Eastern District of Arkansas.

Submitted: April 8, 1985
Filed: August 23, 1985

Before ROSS and JOHN R. GIBSON, Circuit Judges, and MEREDITH,* Senior District Judge.

JOHN R. GIBSON, Circuit Judge.

*The HONORABLE JAMES H. MEREDITH, Senior United States District Judge for the Eastern District of Missouri, sitting by designation.

The issues before us involve a judgment of the district court[1] enjoining the Arkansas Public Service Commission from continuing proceedings to determine whether it should declare void *ab initio* certain contracts entered into by Arkansas Power and Light Company with respect to the purchase of power from, or payment for construction of, a nuclear power plant located in Mississippi. The Arkansas Public Service Commission, the Attorney General of Arkansas, and a consumer group called Ratepayers Fight Back argue that the district court erred in finding that the Federal Energy Regulatory Commission has exclusive jurisdiction over the contracts that were the subject of the APSC's proceedings. They further argue that the district court lacked subject matter jurisdiction, that the litigation was not ripe, and that the court abused its discretion by failing to abstain pending the outcome of the state agency proceedings and by granting overbroad relief. We have carefully considered these arguments, and because we believe that the actions threatened by the APSC would burden interstate commerce, we affirm the judgment of the district court.

The Arkansas Power and Light Company, together with the Louisiana Power and Light Company, the Mississippi Power and Light Company, and New Orleans Public Service, Inc., are wholly-owned operating subsidiaries of Middle South Utilities, Inc. The operating companies provide electric service to wholesale and retail consumers in Arkansas, Louisiana, Mississippi, and Missouri, with an aggregate consumer population of approximately five million people. Planning and operation of the electric generation and transmission facilities needed to meet the demands of the MSU system are performed according to systems agreements. "Transmission and generation functions are so coordinated and integrated as to permit an instantaneous transfer of electrical power to any part of Middle South's transmission network." *Arkansas Power & Light Co. v. Federal Power Commission,* 368

[1]The Honorable Henry Woods, United States District Judge for the Eastern District of Arkansas.

F.2d 376, 378 (8th Cir. 1966). Because the need was seen in the early 1970's to develop additional power generating facilities, Middle South Energy, Inc., also a wholly-owned MSU subsidiary, was created in 1974 to finance, construct, and operate a two-unit nuclear generating plant to be located in Port Gibson, Mississippi and known as the Grand Gulf Nuclear Electric Station.[2] The creation of MSE was necessary because none of the four operating subsidiaries had sufficient resources to finance and construct the nuclear generating plant.

This case involves contracts entered into with respect to the financing and construction of the plant, as well as agreements made concerning the sale of the power to be generated. MSE has financed the three billion dollar cost of the first unit by selling common stock to MSU,[3] borrowing from commercial banks, and issuing first mortgage[4] and pollution control bonds.[5]

[2]Grand Gulf Unit No. 1 was scheduled to commence commercial operation on July 1, 1985, while the construction of Grand Gulf Unit No. 2 has been suspended.

[3]MSU is registered under and subject to Securities and Exchange Commission authority by the Public Utility Holding Company Act of 1935. 15 U.S.C. §§ 79 to 79z-6 (1982). These stock sales received SEC approval. Middle South Utilities, SEC Public Utility Holding Co. Act Rel. No. 23,579 (Jan. 23, 1985). In opposing approval of the most recent stock sale, APSC urged that the SEC withhold authorization until AP&L could show compliance with Arkansas law. The SEC rejected this argument, but assured the APSC that the federal securities authorization did not "supersede requirements of state laws as they may eventually be established in respect to AP&L's commitments in the financing of the Grand Gulf project." *Id.* at 7.

[4]This transaction was approved by the SEC. Middle South Energy, SEC Public Utility Holding Co. Act Rel. No. 23,526 (Dec. 12, 1984).

[5]This transaction was approved by the SEC. Middle South Energy, SEC Public Utility Holding Co. Act Rel. No. 23,495 (Nov. 23, 1984). APSC urged the SEC to withhold approval on the ground that AP&L had not complied with state law. The SEC declined, but noted that the SEC "does not resolve disputed issues of state law and the order in this case does not prejudice the Arkansas Commission, which may assert its jurisdiction under whatever procedures the state laws permit." *Id.* at 2 (footnote omitted).

In 1974, through a document called the Availability Agreement, MSE obtained from each of the MSU operating companies their commitment to purchase power from the Grand Gulf project. The operating companies agreed to pay MSE, beginning on specified dates, amounts needed for MSE to meet its operating expenses, whether or not the two units of the project were then operating. Payments would be credited to the cost of their future power purchases from MSE. The Availability Agreement has been essential to the financing of the project.[6] Pursuant to a series of ten agreements entered into between 1977 and 1984, MSE has assigned its rights under the Availability Agreement to secure indebtedness in excess of $2.5 billion.[7]

The Availability Agreement initially provided that the share of Grand Gulf power taken by the operating companies would vary relative to their respective needs. In June 1981, the Availability Agreement was amended[8] to fix the allocations of power in these percentages:[9] AP&L—17.1%; LP&L—26.9%; MP&L—31.3%; NOPSI—24.7%.

[6]The financing aspects of the original Availability Agreement were approved by the SEC. Middle South Utilities, SEC Public Utility Holding Co. Act Rel. No. 18,437 (June 4, 1974). APSC did not intervene in this proceeding. Its attacks on the agreement in collateral proceedings before the SEC have been rejected. *See supra* notes 3 & 5.

[7]A number of agreements were executed in which the operating companies agreed that in case of default by MSE they would make payments due under the Availability Agreement directly to the banks. In return, the lenders agreed that, should some regulatory agency prohibit the operating companies from making payments under the Availability Agreement, the lenders would make unsecured advances to MSE equal to the amounts it would have received under the Availability Agreement.

[8]The Amendment was approved by the SEC. Middle South Energy, Public Utilities Holding Co. Act Rel. No. 22,098 (June 22, 1981).

[9]South Mississippi Electric Power Association, which is not a subsidiary of MSU, owns 10% of the Grand Gulf project. The allocation figures pertain to the 90% share owned by MSE.

On July 28, 1981, MSE and the operating companies entered into a Reallocation Agreement, under which the operating companies agreed to purchase power in the following percentages: AP&L—0%; LP&L—38.57%; MP&L—31.63%; NOPSI—29.80%.[10] In June 1982, MSE and the operating companies entered into an agreement, the Unit Power Sales Agreement, which required each operating company to purchase the shares of power specified in the Reallocation Agreement. AP&L signed the UPSA but, in accordance with the terms of the Reallocation Agreement, did not agree to purchase any power from the project. The UPSA was filed with the Federal Energy Regulatory Commission for approval as a wholesale power sales agreement.

In February 1984, a FERC administrative law judge rejected the allocation in the UPSA and obligated the operating companies to purchase power from Unit No. 1 as follows: AP&L—36%; LP&L—14%; MP&L—33%; NOPSI—17%. The ALJ reasoned that:

> [T]he evidence of Middle South's witnesses is overwhelming that the Middle South system is a single integrated and coordinated electric system operating in Louisiana, Mississippi, Arkansas and Missouri. Planning, construction, and operations are conducted for the system as a whole. Loads on the system are met by centrally dispatching the most economical mix of generators wherever located in the system. Middle South Utilities, Inc. owns the stock of the operating utilities as well as the stock of MSS and MSE. When difficult system decisions have to be made, such as deciding the allocation of Grand Gulf, it is the Board of Directors of Middle South Utilities, Inc., that ultimately makes the decision, not an individual subsidiary company or a group of subsidiaries.
>
> The Grand Gulf project was initiated in the 1970's to meet the then projected demand on the Middle South system by the end of that decade and not just the load of any Middle South operating company or companies. Constructing generation to meet system load was true of every unit constructed on the Middle South system.
>
> Under these circumstances the costs of Grand Gulf capacity and energy should be shared equitably by MSU's operating companies and their customers.

[10]This agreement was approved by the SEC. Middle South Energy, Public Utility Holding Co. Act Rel. No. 22,280 (Nov. 18, 1981).

Middle South Energy, 26 F.E.R.C. ¶ 63,044, at 65,106 (1984), *aff'd,* 31 F.E.R.C. ¶ 61,305 (1985). The APSC had actively intervened in the proceedings before FERC. It had contended that FERC had no jurisdiction to obligate AP&L to take a share of Grand Gulf and that Arkansas neither wanted or needed the relatively high-cost power from the project. These arguments were rejected.

Approximately one month later, the APSC issued two orders instituting formal inquiries into AP&L's role in the Grand Gulf project. Predicting that Grand Gulf would result in "dramatic [rate] increases" which would place an "intolerable burden" on AP&L's customers and have a "crippling effect" on the Arkansas economy, *Arkansas Power & Light Co.,* Ark. Pub. Serv. Comm'n Docket No. 84-041-0II, at 1 (Mar. 12, 1984), the APSC ultimately sought to "protect the interests of the residential, business, and industrial customers of AP&L and preserve the viability of the economy of the State of Arkansas." *Arkansas Power & Light Co.,* Ark. Pub. Serv. Comm'n Docket No. 84-040-0II, at 2 (Mar. 12, 1984).

On August 1, 1984, the APSC ordered AP&L to appear and "show cause why all contracts and agreements made by it with respect to any obligations to purchase power from or to pay for construction and operation costs of the Grand Gulf Project should not be held to be void *ab initio* as a matter of law." *Arkansas Power & Light Co.,* Ark. Pub. Serv. Comm'n Docket No. 84-190-U, at 6 (Aug. 1, 1984). The APSC had already concluded that thirty-six such agreements constituted prima facie violations of

Arkansas law requiring APSC approval of certain transactions by public utilities. *Id.; see* Ark. Stat. Ann. § 73-253(a)(3) (1979 Repl.) (utility must have APSC approval to "sell, acquire, lease or rent any public utility plant or property constituting an operating unit or system"); *id.* § 73-255 (Supp. 1983) (utility must have APSC approval to "issue stocks, bonds, notes or other evidence of indebtedness payable at periods of more than thirty-six (36) months"). After AP&L's motion to dismiss the show cause order for lack of jurisdiction was denied, MSE filed suit in the district court to temporarily and permanently enjoin the proceedings before the APSC. AP&L intervened as a plaintiff, while the Arkansas Attorney General and Ratepayers Fight Back intervened as defendants. A hearing was held on the consolidated issues of preliminary and permanent relief. The district court found that the APSC's actions were preempted by the Federal Power Act, 16 U.S.C. §§ 824–824K (1982), and permanently enjoined APSC from conducting further proceedings on the show cause order. Regarding the need for equitable relief, the court found:

> MSE must raise an additional several billion dollars in the next few years to pay construction and financing costs. The ability to raise these funds is dependent on the enforceability of the threatened agreements. If the actions of the APSC are not enjoined, the cost of capital to MSE will be raised to the point that the Project is jeopardized, and the ability of MSE to provide its multi-state wholesale customers with power will be irreparably impaired.

Middle South Energy, Inc. v. Arkansas Public Service Commission, No. LR-C-84-778, slip op. at 5 (E.D. Ark. Sept. 14, 1984).[11]

The APSC, the Arkansas Attorney General, and Ratepayers filed an appeal with this court.[12] After the case was argued, FERC

[11]The SEC noted recently that delaying commercial operation of the reactor would increase costs by about $28 million per month, primarily in finance charges. Middle South Utilities, Public Utility Holding Co. Act Rel. No. 23,579 at 9 (Jan. 23, 1985).

[12]Arkansas Electric Energy Consumers and Reynolds Metals Company filed an amicus curiae brief, as did the Metropolitan Life Insurance Company and other holders of MSE's first mortgage bonds.

affirmed the order of the ALJ allocating AP&L 36% of the Grand Gulf capacity. *Middle South Energy,* 31 F.E.R.C. ¶ 61,305 (1985).

I.

As an initial matter, amicus curiae on behalf of the APSC[13] asserts that MSE's suit does not "aris[e] under the Constitution [or] laws *** of the United States" as required to invoke federal question jurisdiction under 28 U.S.C. § 1331 (1982) because, pursuant to the "well-pleaded complaint" rule, the federal question must be raised necessarily as an element of the plaintiff's entitlement to relief and cannot merely be a response to an anticipated defense. *See generally Franchise Tax Board v. Construction Laborers Vacation Trust,* 463 U.S. 1, 7–12 (1983) (citing older cases). Specifically, amicus curiae argues that jurisdiction is lacking because MSE's preemption claim is merely a defense to the state administrative action. *See id.* at 15–16 (discussing *Skelly Oil Co. v. Phillips Petroleum Co.,* 339 U.S. 667 (1950)). This argument ignores the recognition by the Supreme Court that "a claim of federal preemption does not always arise as a defense to a coercive action." *Franchise Tax,* 463 U.S. at 12 n.12; *see Aluminum Co. of America v. Utilities Commission,* 713 F.2d 1024, 1028 (4th Cir. 1983), *cert. denied,* 104 S. Ct. 1326 (1984). The "not a defense to a state action" rule is premised on the determination that the declaratory judgment act, 28 U.S.C. § 2201 (1982), is merely procedural and that Congress thereby did not enlarge the subject matter jurisdiction of federal courts. *Skelly Oil Co. v. Phillips Petroleum Co.,* 339 U.S. 667, 671–72 (1950). This concern is not implicated when the declaratory plaintiff has independent grounds for federal relief such as an injunction. Note, *Federal Jurisdiction over Declaratory Suits*

[13]We consider this issue, though not raised by a party, since subject matter jurisdiction cannot be waived or conferred by consent. *Insurance Corp. of Ireland v. Compagnie des Bauxites de Guinea,* 456 U.S. 694, 702 (1982); *United States ex rel. Burnette v. Driving Hawk,* 587 F.2d 23, 24 (8th Cir. 1978).

Challenging State Action, 79 Colum. L. Rev. 983, 1001 (1979).[14] Thus, the district court had subject matter jurisdiction pursuant to MSE's complaint, which on its face properly raises the federal question of whether the state proceeding should be enjoined on preemption[15] grounds.[16] *Shaw v. Delta Air Lines,* 463 U.S. 85, 96 n.14 (1983).

[14]To deny access to federal court when, regardless of the existence of procedures for declaratory relief, an injunction would otherwise have been available would contract the jurisdiction of the federal courts. Note, *supra,* at 1001. Cases that appear to have taken this route have generally relied on the Supreme Court decision of *Public Serv. Comm'n v. Wycoff Co.,* 344 U.S. 237 (1952), which actually turned on the failure of the plaintiff to establish a ripe controversy or to identify what right it was asking the court to declare. *Id.* at 244–46; *see Franchise Tax,* 463 U.S. at 16 n.14. Furthermore, the widely quoted *Wycoff* dictum suggesting that even if the controversy had been ripe, federal subject matter jurisdiction would have been lacking, is again couched solely in terms of declaratory relief, the Court having determined that the plaintiff had abandoned its request for an injunction because of the absence of proof of the threatened injury necessary to support that form of relief. 344 U.S. at 241. The Supreme Court itself has never interpreted *Wycoff,* as some courts of appeals have, to hold that subject matter jurisdiction does not exist any time a federal claim can be litigated as a state defense. *Illinois v. General Elec. Co.,* 683 F.2d 206, 211 (7th Cir. 1982), *cert. denied,* 461 U.S. 913 (1983); *Braniff Int'l v. Florida Pub. Serv. Comm'n,* 576 F.2d 1100, 1104 (5th Cir. 1978). Concerns with the timing of adjudication need not distort analysis of subject matter jurisdiction but instead can be—and more appropriately are—handled through the discretion of courts in matters involving equitable relief and through doctrines such as exhaustion of administrative remedies and abstention. Note, *supra,* at 1001.

[15]It makes no difference to subject matter jurisdiction that we ultimately choose not to decide this case on preemption grounds. Furthermore, the operation of the commerce clause in limiting state authority is sufficiently similar to preemption that we believe the same jurisdictional analysis applies.

[16]There are no Eighth Circuit decisions to the contrary. Despite the representations of amicus curiae, three of the cases it cites stand only for the proposition that a preemption claim does not raise a federal question under section 1331 when, ***absent the availability of the declaratory judgment procedure,*** it would have arisen only as a defense to a state ac-

(Footnote continued on next page.)

Appellants nevertheless argue that jurisdiction is lacking because there will be no "ripe" case or controversy until the APSC reaches some determination as to the validity of the contracts and the effects of that determination are felt by MSE. *See Abbott Laboratories v. Gardner,* 387 U.S. 136, 148–49 (1967). This argument again ignores the true nature of the relief sought. MSE challenges not the state's ultimate substantive decision but its authority to even conduct the contemplated proceeding. It can hardly be doubted that a controversy sufficiently concrete for judicial review exists when the proceeding sought to be enjoined is already in progress.

II.

The district court's decision on preemption grounds was based on the Federal Power Act. Congress's purpose in enacting the Act was to regulate "the transmission of electric energy in interstate commerce and *** the sale of electric energy at wholesale in interstate commerce." 16 U.S.C. § 824(b) (1982). To accomplish this goal, Congress gave FERC the power to make "just and reasonable" any public utility "rule, regulation, practice *or contract*

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tion. Neither the language nor context of these cases extends this interpretation of the well-pleaded complaint rule to foreclose *injunctions* sought on preemption grounds. *E.g., First Fed. Sav. & Loan Ass'n v. Anderson,* 681 F.2d 528 (8th Cir. 1982) (declaratory judgment only sought; no pending state proceeding to enjoin); *Lawrence County v. South Dakota,* 668 F.2d 27 (8th Cir. 1982) (same); *First Nat'l Bank v. Aberdeen Nat'l Bank,* 627 F.2d 843 (8th Cir. 1980) (en banc) (removal to federal court improper when based on ground that preemption would be raised as a defense to state tort action). The one case cited by amicus curiae in which we did find subject matter jurisdiction lacking despite a request for an injunction is distinguishable in that the panel expressly found the preemption claim there to be only in the nature of a defense to the state administrative proceeding. *Home Fed. Sav. & Loan Ass'n v. Insurance Dep't,* 571 F.2d 423, 427 (8th Cir. 1978). Since MSE is seeking affirmative relief from the APSC's attempts to even inquire into certain affairs relating to its business, we need not decide if the characterization of the preemption claim in *Home Federal* remains viable in light of *Shaw.*

affecting [a] rate, charge, or classification [that] is unjust, unreasonable, unduly discriminatory or preferential." *Id.* § 824e(a) (emphasis added).

The district court held that the Availability Agreement and its amendments were "agreements for the purchase of wholesale power in interstate commerce or are so integrally related to such purchases that they are subject to the exclusive jurisdiction of the FERC." Slip op. at 7. The other agreements subject to the APSC order were found to be "essential to the interstate wholesale sale of power and therefore *** not subject to state jurisdiction." *Id.* We read the district court's order as finding preemption on the ground that the threatened actions of the APSC would block the accomplishment of the purpose behind the Federal Power Act. *See Hines v. Davidowitz,* 312 U.S. 52, 67 (1941).

Essentially, the APSC is trying to secure for Arkansas the zero allocation embodied in the UPSA. Such a result would be contrary to the 36% allocation recently approved by FERC in regulating the wholesale aspects of the Grand Gulf project. Thus, a strong argument can be made that the APSC's powers have been preempted by the Federal Power Act. The appellants, on the other hand, urge that we examine the APSC's powers in light of other federal legislation, the Public Utility Holding Company Act of 1935. This law, they argue, expressly reserves to the states some jurisdiction to regulate the securities dealings of utility holding companies and their subsidiaries. *See* 15 U.S.C. §§ 79f(b), 79g(g), 79u (1982); *infra* at 17-20; *supra* notes 3 & 5.

The district court's order did not squarely deal with the argument now made by appellants. We are not convinced that the district court improperly based its decision on preemption grounds. Nevertheless, we choose not to address the difficult question of whether the authority denied the states under the Federal Power Act may be granted to them by the Holding Company Act, because the case can be disposed of under well-settled commerce

clause principles. *See New England Power Co. v. New Hampshire,* 455 U.S. 331, 344 n.10 (1983) (deferring resolution of preemption issues in favor of commerce grounds).

III.

The commerce clause grants Congress the power to regulate commerce among the states. U.S. Const., art. I, § 8, cl. 3. It has long been recognized as implying limits on the powers of the states to erect barriers against interstate trade. *South-Central Timber Development v. Wunnicke,* 104 S. Ct. 2237, 2240 (1984); *see Cooley v. Board of Wardens,* 53 U.S. (12 How.) 299, 317-18 (1852). Absent conflicting federal legislation, the states may exercise police power over matters of legitimate local concern even though such regulation may affect interstate commerce. *Philadelphia v. New Jersey,* 437 U.S. 617, 623-24 (1978); *Raymond Motor Transportation v. Rice,* 434 U.S. 429, 440 (1978). Incidental burdens on interstate commerce may be unavoidable when a state legislates to protect its citizens. *Philadelphia* v. *New Jersey,* 437 U.S. at 623-24. Nevertheless, the safeguarding of local interests must ultimately yield to the principle that "one state in its dealings may not place itself in a position of economic isolation." *Baldwin v. G.A.F. Seeling, Inc.,* 294 U.S. 511, 527 (1935).

"[T]he regulation of utilities is one of the most important of the functions traditionally associated with the police power of the states." *Arkansas Electric Cooperative Corp. v. Arkansas Public Service Commission,* 461 U.S. 375, 377 (1983). "Need for new power facilities, their economic feasibility, and rates and services, are areas that have been characteristically governed by the States." *Pacific Gas & Electric Co. v. State Energy Resources Conservation & Development Commission,* 461 U.S. 190, 205 (1983); *see also Central Hudson Gas & Electric Corp. v. Public Service Commission,* 447 U.S. 557, 569 (1980) ("The state's con-

cern that rates be fair and efficient represents a clear and substantial governmental interest."). At the same time, however, the "production and transmission of energy is an activity particularly likely to affect more than one state, and its effect on interstate commerce is often significant enough that uncontrolled regulation by the States can patently interfere with broader national interests." *Arkansas Electric*, 461 U.S. at 377. The dispositive issue here is whether the APSC's desire to protect Arkansas' interest has resulted in an impermissible burden on interstate commerce.

IV.

The Attorney General argues that since the APSC has only issued a show cause order, and not actually voided the contracts in issue, there is no significant burden on interstate commerce. The APSC's position in the administrative proceedings surrounding Grand Gulf, however, leaves little doubt that APSC intends to substantially reduce or eliminate AP&L's participation in the project. The threat of enforcement presented by the show cause order is sufficient to support an injunction against further proceedings.

On March 12, 1984, the APSC issued two orders instituting investigations. The first, retrospective in nature, referred to developments in FERC proceedings that "portend[ed] catastrophically enormous rates increases" for AP&L customers. *Arkansas Power & Light Co.*, Ark. Pub. Serv. Comm'n Docket No. 84-040-0II, at 1 (Mar. 12, 1984). The second order, prospective in nature, was to

> look forward to ascertain what the ratepayers of AP&L, AP&L itself, the Commission, the Governor, and the General Assembly may do to circumvent or deflect the economic harm that looms over the State from the imminent prospect of being mandated by a federal agency to pay for a power generating plant that is possibly neither needed or wanted by anyone in Arkansas, * * * and that would, if forced upon the State, potentially result in such immense amounts of excess generating capacity that it could neither be used or sold by AP&L.

Arkansas Power & Light Co., Ark. Pub. Serv. Comm'n Docket No. 84-041-0II, at 2 (Mar. 12, 1984); *see supra* at 6.

Nearly five months later, APSC issued the show cause order that gave rise to this lawsuit. It listed thirty-six agreements relating to the Grand Gulf project, and stated: "The construction of the Grand Gulf Project was and is dependent on the[se] agreements." *Arkansas Power & Light Co.*, Ark. Pub. Serv. Comm'n Docket No. 84-190-U, at 5 (Aug. 1, 1984). The APSC stated that its approval, required by Arkansas law, had not been given the agreements and that some or all were "prima facie violations of Arkansas law." *Id.* at 6. AP&L was ordered to appear and show cause "why all contracts and agreements made by it with respect to any obligations to purchase power from or to pay for construction and operation costs of the Grand Gulf Project should not be held void *ab initio* as a matter of law." *Id.* The APSC later denied AP&L's motion to dismiss the show cause order for lack of jurisdiction based on FERC's exclusive jurisdiction over the agreements. *Arkansas Power & Light Co.*, Ark. Pub. Serv. Comm'n Docket No. 84-190-U (Aug. 31, 1984).

The APSC argued vigorously before both FERC and the SEC for a reduction or elimination of AP&L's role in Grand Gulf. In an SEC proceeding to authorize the sale of common stock by MSE, the APSC asked the Commission to consider the "discontinuance or moth-balling" of the Grand Gulf project. Middle South Utilities, SEC Public Utility Holding Co. Act Rel. No. 23,579 at 9 (Jan. 23, 1985). In litigation before FERC, the APSC sought to avoid the allocation of any Grand Gulf power to Arkansas, claiming that the state does not need and cannot economically use the power. *Middle South Energy*, 26 F.E.R.C. ¶ 63,044 (1984), *aff'd*, 31 F.E.R.C. ¶ 61,305 (1985).[17]

[17]Further, after this lawsuit was filed, the following account appeared in the press: "[A]n attorney representing the Arkansas utility commis-

(Footnote continued on next page.)

The threat posed by the show cause order is sufficient to warrant the injunction. In *Pennsylvania v. West Virginia*, 262 U.S. 553 (1923), two states brought suits to enjoin West Virginia from enforcing legislation that would have reduced out-of-state delivery of West Virginia natural gas. The Court rejected the argument that the suits were premature, finding that the gas curtailment was "presently threatened and likely to be productive of great injury." *Id.* at 591. In proceeding to consider the merits of the commerce clause issue, the Court observed: "One does not have to await the consummation of threatened injury to obtain preventive relief. If the injury is certainly impending that is enough." *Id.* at 593; *see also Pacific Gas & Electric Co. v. State Energy Resources Conservation & Development Commission*, 461 U.S. 190, 201 (1983) (decision on preemption of state nuclear waste disposal law should not be delayed because postponement "would likely work substantial hardship on the utilities").

The mere possibility that a state's interpretation of its law may avoid the necessity for an injunction does not preclude federal review. In *City of Chicago v. Atchison, Topeka & Santa Fe Railway*, 357 U.S. 77 (1958), the Court rejected an argument in a commerce clause case that a declaratory judgment should not issue because the state courts had not been given a chance to act. Among other things, the Court reasoned that: "Remission to [state court] would involve substantial delay and expense, and the chance of a result different from that reached below, on the issue of applicability, would appear to be slight." *Id.* at 84.

In this case, as in the *West Virginia* and *Pacific Gas* cases, the threatened action is likely to cause great injury, in the form of higher financing costs for MSE. Also, as in *City of Chicago*, the

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sion said the commission staff is confident it can defend its order against the Middle South suit. He added that "if the APSC voids AP&L's part (of Grand Gulf), the whole thing goes down the toilet." Wall St. J., Sept. 6, 1984, at 7, col. 4-5 (Plaintiff's Ex. 10).

chance of a state adjudication obviating the commerce clause issue is remote. Thus, we conclude that a commerce clause violation can be found notwithstanding that the APSC has not actually voided the agreements. *Cf. Northern Natural Gas Co. v. State Corporation Commission*, 372 U.S. 84, 92 (1963) ("[A]lthough collision between the state and federal regulation may not be an inevitable consequence, there lurks such imminent possibility of collision in orders purposely directed at interstate wholesale purchasers that the orders must be declared a nullity."); *Public Service Commission v. Wycoff Co.*, 344 U.S. 237, 245 (1952) (Court refused to allow suit for declaratory relief against state commission where no "risk of suffering penalty, liability or prosecution was shown"); *Natural Gas Pipeline Co. v. Slattery*, 302 U.S. 300, 308-09 (1937) (declining to find a commerce clause violation in utilities commission merely seeking records, the Court noted that no action based on discovered information was alleged and that it "will be time enough to challenge such action of the commission when it is taken or *at least threatened*") (emphasis added) (citations omitted).

V.

We next consider appellants' argument that Congress has authorized any unconstitutional effect that the APSC's actions may have on interstate commerce. Congress may confer upon the states the ability that they would otherwise not enjoy to restrict the flow of interstate commerce. *Lewis v. BT Investment Managers*, 447 U.S. 27, 44 (1980); *Southern Pacific Co. v. Arizona*, 325 U.S. 761, 769 (1945). "But when Congress has not 'expressly stated its intent and policy' to sustain state legislation from attack under the Commerce Clause, we have no authority to rewrite its legislation based on mere speculation as to what Congress 'probably had in mind.' " *New England Power Co. v. New Hampshire*, 455 U.S. 331, 343 (1982) (quoting *Prudential Insurance Co. v. Benjamin*, 328 U.S. 408, 427 (1946)); *United States v. Public Utilities Commission*, 345 U.S. 295, 319 (1953) (Jackson, J.,

concurring)). Rather, "for a state regulation to be removed from the reach of the dormant commerce clause, congressional intent must be unmistakably clear." *South-Central Timber Development v. Wunnicke*, 104 S. Ct. 2237, 2242 (1984).

Ratepayers urge that there has been an "explicit recognition by Congress of the authority of a state to regulate the securities of an electric utility operating within its borders." It is true that the Public Utility Holding Company Act of 1935 (HCA), 15 U.S.C. §§ 79 to 79z-6 (1982), expressly reserves some regulatory powers to the states. Nevertheless, the provisions that Ratepayers rely upon show no congressional purpose to insulate the APSC's activity from commerce clause scrutiny.

The HCA generally requires registered companies and their subsidiaries to file declarations with the SEC that must be approved before securities may be issued or sold. 15 U.S.C. §§ 79f, 79g. Section 79f(b) exempts from the declaration requirement securities of a subsidiary company of a registered holding company, "if the issue and sale * * * are solely for the purpose of financing the business of such subsidiary company and have been expressly authorized by the State Commission of the state in which such subsidiary company is organized and doing business." This narrow exemption obviously envisions a transaction completely different from the Grand Gulf agreements. The documents of concern to the APSC involve all the entities in the Middle South system. They implicate interstate commerce far more than the intrastate dealings between a state commission and a single subsidiary do. Thus, we find in section 79f(b) no express statement by Congress to exempt the APSC's activity from the commerce clause.

A related provision, section 79g(g), provides for state input during the SEC's consideration of proposed declarations:

> If a State commission or State securities commission having jurisdiction over any of the acts enumerated in subsection

> (a) of section 79f of this title, shall inform the Commission * * * that State laws applicable to the act in question have not been complied with, the Commission shall not permit a declaration * * * to become effective until and unless the Commission is satisfied that such compliance has been effected.

Like section 79f(b), this section contains no direction from Congress concerning immunity from the commerce clause.

These conclusions are supported by *New England Power Co. v. New Hampshire*, 455 U.S. 331 (1982). In *New England Power*, the Court considered the relationship of the commerce clause to the Federal Power Act. A state utilities commission had sought to restrict the export of hydroelectric energy generated within the state. The state claimed that this action was not invalid under the commerce clause because a section in the Federal Power Act provided that the Act "shall not * * * deprive a State or State commission of its lawful authority now exercised over the exportation of hydroelectric energy which is transmitted across a State line." *Id.* § 824(b). The Court interpreted this section as doing nothing more than saving from federal preemption state authority that was otherwise lawful. It concluded that section 824(b)

> is in no sense an affirmative grant of power to the states to burden interstate commerce "in a manner which would otherwise not be permissible." * * * Nothing in the legislative history or language of the statute evinces a congressional intent "to alter the limits of state power otherwise imposed by the Commerce Clause," or to modify the earlier holdings of this Court concerning the limits of state authority to restrain interstate trade. Rather, Congress' concern was simply "to define the extent of the federal legislation's pre-emptive effect on state law."

455 U.S. at 341 (citations omitted).

The provisions of the HCA discussed above are facially similar to the statute at issue in *New England Power*. Moreover, the

Federal Power Act and the HCA have similar legislative histories. *Compare New England Power,* 455 U.S. at 341 ("The legislative history of the [Federal Power] Act * * * indicates that Congress intended only that its legislation '*tak[e] no authority from* State commissions.' ") (quoting H.R. Rep. No. 1318, 74th Cong., 1st Sess. 8 (1935)), *with Alabama Electric Cooperative v. Securities & Exchange Commission,* 353 F.2d 905, 907 (D.C. Cir. 1965) ("The purpose of the Public Utility Holding Company Act, as shown by its legislative history, was to supplement state regulation—not to supplant it."). Thus, sections 79f(b) and 79g(g) do not preclude us from finding a violation of the commerce clause here.

Ratepayers also contend that 15 U.S.C. § 79u saves any commerce clause transgression. This section provides:

> [N]or shall anything in this chapter affect the jurisdiction of any other commission, board, agency or officer of * * * any state or political subdivision of any State, over any person, security, or contract, insofar as such jurisdiction does not conflict with any provision of this chapter or any rule, regulation, or order thereunder.

In *Edgar v. Mite Corp.,* 457 U.S. 624 (1982), the Supreme Court considered whether a state tender offer statute violated the commerce clause. The federal securities laws contained a provision nearly identical to section 79u. *See* 15 U.S.C. § 78bb(a) (1982). There was no suggestion made that this savings provision could authorize state violations of the commerce clause. Rather, Justice White interpreted the statute as leaving to the courts to decide whether similar state legislation may be preempted. 457 U.S. at 631. Although Justice White did not speak for the whole Court, *Mite* supports a conclusion that section 79u does not insulate the APSC's actions from examination under the commerce clause.

VI.

We must next determine the appropriate level of scrutiny under the commerce clause. The Supreme Court has recently applied two tests to state restrictions on the flow of interstate power. In *New England Power Co. v. New Hampshire,* 455 U.S. 331 (1982), the New Hampshire Public Utilities Commission sought to restrict the export of hydroelectric energy produced within the state. The Commission's purpose was to contain the cost savings associated with this cheaper form of electrical generation to the citizens of New Hampshire. This savings was to be obtained at the expense of customers in neighboring states that had been sharing the power produced in New Hampshire. *Id.* at 335–36, 339. The Supreme Court had no trouble concluding that this sort of "protectionist regulation" was forbidden by the commerce clause. *Id.* at 339. Two reasons were cited for reaching this result. First, the utilities commission had made clear that its order was "designed to gain an economic advantage for New Hampshire citizens at the expense of * * * customers in neighboring states." *Id.* Second, the Court found indisputable that the " 'exportation ban' place[d] direct and substantial burdens on transactions in interstate commerce." *Id.* (citing *Public Utilities Commission v. Attleboro Steam & Electric Co.,* 273 U.S. 83 (1927)). There was no discussion of balancing the state's interest against the detriment to interstate commerce.

A different analysis was used the next year in *Arkansas Electric Cooperative Corp. v. Arkansas Public Service Commission,* 461 U.S. 375 (1983). At issue was an order of the APSC asserting jurisdiction over the wholesale rates charged retail distributors by a rural power cooperative. The cooperative argued that this assertion violated the commerce clause under the test articulated in *Attleboro,* which invalidated regulations imposing a "direct" rather than "indirect" burden on interstate commerce. 461 U.S. at 390; *see Attleboro,* 273 U.S. at 90. The Court, however, decided to apply "an analysis grounded more solidly" in modern com-

merce clause cases: "Where [a] statute regulates evenhandedly to effectuate a legitimate local public interest, and its effects on interstate commerce are only incidental, it will be upheld unless the burden imposed on such commerce is clearly excessive in relation to the putative local benefits." 461 U.S. at 393–94 (quoting *Pike v. Bruce Church,* 397 U.S. 137, 142 (1970)). After applying this test, the Court upheld the APSC's assertion of jurisdiction.

Thus, the Court has applied a rule of presumptive invalidity to regulations designed to further economic protectionism, and a balancing test, which is far more deferential to the states, to facially neutral regulations. *See generally Baltimore Gas & Electric Co. v. Heintz,* 760 F.2d 1408, 1420–22 (4th Cir. 1985) (discussing flux in commerce clause jurisprudence). *New England Power* and *Arkansas Electric* can be harmonized under the following standard: "[W]here simple economic protectionism is effected by state legislation, a virtual *per se* rule of invalidity has been erected. In contrast, legislation that visits its effects equally upon interstate and local business may survive constitutional scrutiny if it is narrowly drawn." *Lewis v. BT Investment Managers,* 447 U.S. 27, 36 (1980). The "crucial inquiry," therefore, is whether the APSC's action "is basically a protectionist measure, or whether it can fairly be viewed as a law directed to legitimate local concerns, with effects upon interstate commerce that are only incidental." *Philadelphia v. New Jersey,* 437 U.S. 617, 624 (1978). If a discriminatory purpose is found, there is no need to engage in the *Bruce Church* balancing approach. *Bacchus Imports, Ltd. v. Dias,* 104 S. Ct. 3049, 3055 (1984).

"A finding that state legislation constitutes 'economic protectionism' may be made on the basis of either discriminatory purpose or discriminatory effect." *Id.* In this case, there is ample evidence of both. The APSC seeks to cancel the Grand Gulf agreements ostensibly because they have not received the necessary state regulatory approval. Its apparent concern, which has been made abundantly plain in its orders and its arguments before the SEC

and FERC, however, is the economic impact on Arkansas citizens caused by AP&L's participation in Grand Gulf. It seeks to deflect what it has estimated to be rate increases of more than $3.5 billion over the next ten years.[18] Given free rein, the APSC would shift this burden to the citizens of Mississippi and Louisiana, citizens who are powerless to directly influence Arkansas' internal affairs.

In *New England Power,* New Hampshire sought to contain within the state the benefits of low-cost power. Arkansas, conversely, seeks to close its borders to high-cost electricity. The effect of both actions is the same: a preference for citizens in the regulating jurisdiction gained at the expense of out-of-state customers. Nor can it be doubted that the APSC's action would constitute a direct and substantial burden on interstate commerce. The integrated nature of MSU and MSE, particularly the Grand Gulf project, represents commerce that is interstate in a most basic form. Thus, this case is controlled by *New England Power,* and the APSC must be prohibited from voiding AP&L's role in the Grand Gulf project. *See also Philadelphia v. New Jersey,* 437 U.S. at 624 ("The clearest example of [protectionist] legislation is a law that overtly blocks the flow of interstate commerce at a state's borders.").[19]

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[18]*See Middle South Energy,* 26 F.E.R.C. at 65,097:

Because the costs of power from Grand Gulf are perceived to be much higher than the costs of power from other sources on the MSU system, it is not surprising that each of these parties supports an allocation of power which results in the lowest allocation to the MSU operating company or companies in which the party is interested, especially during the early years of operation of Grand Gulf when the costs of Grand Gulf are higher than in later years.

[19]The APSC's reliance on *Indiana & Mich. Power Co. v. Michigan,* 405 Mich. 400, 275 N.W.2d 450 (1979), is misplaced, for that case did not involve state regulation with protectionist motives. *See Michigan Gas Storage Co. v. Michigan Pub. Serv. Comm'n,* 405 Mich. 376, 275 N.W.2d 457 (1979) (companion case).

VII.

Finally, appellants assert that the district court should have used its discretion to withhold the exercise of its powers under any of several doctrines concerned with premature federal interference with state proceedings.

Under *Burford v. Sun Oil Co.*, 319 U.S. 315 (1943), for example, a federal court should abstain when the action before it involves matters of state law best left to the state alone. The very premise of this doctrine, however, is lacking when, as here, federal law or Constitution makes the proceeding or regulation at issue beyond the state's authority. *South Central Bell Telephone Co. v. Louisiana Public Service Commission*, 744 F.2d 1107, 1123–24 (5th Cir. 1984), *petition for cert. filed*, 53 U.S.L.W. 3449 (U.S. Nov. 30, 1984) (No. 84-870). There is no concern with protecting a legitimate state regulatory scheme, *Baggett v. Department of Professional Regulation*, 717 F.2d 521, 524 (11th Cir. 1983), and the question becomes one of basic federal supremacy, which does not turn on local factors or local expertise. *South Central Bell*, 744 F.2d at 1123.

Similarly, the rule of *Younger v. Harris*, 401 U.S. 37 (1971), limiting injunctions of pending state proceedings embodies the principle of our federal system that legitimate state functions be respected.[20] This "comity," however, is not strained when a federal court cuts off state proceedings that entrench upon the federal domain. *Baggett*, 717 F.2d at 524. The legitimate state interest contemplated by *Younger*, *see Middlesex County Ethics Committee v. Garden State Bar Association*, 457 U.S. 423, 432 (1982), does not exist when the state action has been preempted

[20]Because of our ultimate conclusion, we may assume without deciding that the *Younger* doctrine, which was developed in the context of state criminal proceedings, applies to the show cause order and proceedings contemplated by the Arkansas Public Service Commission. *See generally Middlesex County Ethics Comm. v. Garden State Bar Ass'n*, 457 U.S. 423, 432 (1982) (discussing scope of *Younger*).

or foreclosed by the Constitution. *Champion International Corp. v. Brown*, 731 F.2d 1406, 1408 (9th Cir. 1984).

Abstention under *Railroad Commission v. Pullman Co.*, 312 U.S. 496 (1941), focuses on whether a decision by a state court might clarify state law so as to make it unnecessary to reach a constitutional issue otherwise presented. Preemption and the commerce clause, however, are matters of federal law, and there is no interpretation of Arkansas law which could make it unnecessary for us to reach the question as to whether the Constitution forecloses even the mere issuance of the show cause order entered here by the APSC. *See Hotel & Restaurant Employees Union Local 54 v. Danziger*, 709 F.2d 815, 832 (3d Cir. 1983), *vacated on the merits sub nom. Brown v. Hotel & Restaurant Employees Union Local 54*, 104 S. Ct. 3179 (1984).

Finally, the doctrine of exhaustion of administrative remedies in the context of state agency proceedings simply addresses many of the same concerns which the various types of abstention are designed to reach. *See* 4 K. Davis, *Administrative Law Treatise* § 25:1, at 350 (1983); *see also West v. Bergland*, 611 F.2d 710, 715–17 (8th Cir. 1979) (developing factors used in determining whether to require exhaustion), *cert. denied*, 449 U.S. 821 (1980).

To the degree that irreparable harm also must be shown, *see West*, 611 F.2d at 719–20, MSE alleges such injury in the form of loss through exhaustion of the very right—the right to be free of the state administrative proceeding—it seeks to protect. The Supreme Court recognized such a right on similar facts in *Public Utilities Commission v. United Fuel Gas Co.*, 317 U.S. 456 (1943), when an interstate gas supplier sought to enjoin the enforcement against it of a state agency order requiring it to prove the reasonableness of the rates it charged a customer utility within that state. Although the agency had done nothing to that point but assert jurisdiction, *id.* at 465, the Court upheld the injunction

on the ground that the supplier suffered injury from the enforcement of the order for proof itself and that the expense of complying with such orders was among the contingencies against which Congress sought to guard in creating exclusive federal jurisdiction. *Id.* at 469; *see also Public Utilities Commission v. United States,* 355 U.S. 534, 540 (1958) ("But where the only question is whether it is constitutional to fasten the administrative procedure onto the litigant, the administrative agency may be defied and judicial relief sought as the only effective way of protecting the asserted constitutional right."); *Panhandle Eastern Pipe Line Co. v. Public Service Commission,* 332 U.S. 507, 512 (1947) (state agency order requiring interstate gas supplier to file certain tariffs, rules, and regulations was not just a threat to apply the state regulatory plan but constituted actual application of the plan in its initial stages); *cf. Monahan v. Nebraska,* 645 F.2d 592, 597 (8th Cir. 1981) (claim that state procedure itself conflicted with federal act could not be effectively addressed by exhausting state procedure).

Here the mere assertion of jurisdiction by the APSC had a negative impact on MSE's ability to obtain investors and complete its project, thus similarly interfering with the exclusive federal scheme for governing interstate power transmission and sales. And, as in *United Fuel,* we observe that MSE raised the preemption question before the APSC in a motion to dismiss the show cause order for lack of jurisdiction and only filed this suit when such motion was denied. 317 U.S. at 470 (distinguishing *Natural Gas Pipeline Co. v. Slattery,* 302 U.S. 300 (1937)). We thus conclude that neither the failure of MSE to pursue further state remedies nor the abstention doctrines of *Burford, Younger,* or *Pullman* make the district court's resolution of this case an abuse of discretion. Nor are we convinced that the district court improperly determined the need for equitable relief or the scope of the injunction.

The judgment of the district court is affirmed.

APPENDIX M

Supplement To Rule 28.1

Statement

FIRMS (OTHER THAN WHOLLY-OWNED SUBSIDIARIES) IN WHICH ALUMINUM COMPANY OF AMERICA HAS OWNERSHIP INTERESTS

Adela Investment Company S.A.
Alcoa Aluminio S.A.
Alcoa Aluminio do Nordeste S.A.—ALCONOR
Alcoa Mineracao S.A.
Mineracao Ceu Estrelado Limitada
Alumar Administracao De Bens S.A. (Realumar)
Alumar Administracao Industrial S.A. (Alumar)
Companhia Geral De Minas
Imobiliaria Vargem Dos Bois S/C Ltda.
Empresa Imobiliaria Maranhense Ltda.
Alcoa-NEC Communications Corp.
Alcoa Nederland B.V.
Alumet Etten B.V.
Intal B.V.
Lips-Levolor B.V.
Alcoa of Australia Limited
A.F.P. Pty. Limited
Alcoa (Bunbury) Pty. Limited
Alcoa of Australia (Asia) Limited
Coala Insurance Company Limited
Dowell Australia Limited
Acme Metal Works, Ltd.
Dowell Brett Pty. Limited
T.G.A. Pty. Limited
The Glass & Aluminium Suppliers Pty. Limited
Portland Smelter Services Pty. Ltd.
Alcoa of Great Britain Limited
Alcoa Manufacturing (G.B.) Limited
MRCP Limited
Aluwhite Electropaint Limited
Alcoa Conductor Accessories, Inc.

Alcoa Fujikura Ltd.
Aludril, Inc.
Aludrum B.V.
Lamitref Aluminium N.V.
Pimalco, Inc.
Drumalu B.V.
Forges de Bologne
Hopewell International Insurance Ltd.
United Insurance Company
Universal Insurance Company of Ireland Limited
Delta International Insurance Company Limited
Delta Holdings, Inc.
Delta America Re Insurance Company
Delta International Insurance Company Limited
Lancer Financial Group
Delaney Management Company, Inc.
Lancer Insurance Company
Transit Casualty Syndicate, Inc.
Aguas Industriales "La Presa" A.C.
Capsulas Metalicas, S.A.
Complejo Industrial Pedernales, S.A.
Corporation For Innovation Development (CID)
Furukawa Aluminum Co., Ltd.
Abe Kogyo Kabushiki Kaisha
Atsugi Aluminum Kogyo Kabushiki Kaisha
Fuji Aluminum Tube Industries, Ltd.
Fujiko Co., Ltd.
Futaba Trading Co., Ltd.
Higashi Nippon Forging Co., Ltd.
Hino Motors, Ltd.
K. K. Kanagawa Alumi Center
Kanehiro Co., Ltd.
Kohmi Metals Co., Ltd.
Light Metal Extrusion Development Company, Ltd.
Meiji Aluminum Co., Ltd.

Nippon Laminate Co., Ltd.
Nippon Light Metal Mfg. Co., Ltd.
Nippon Foil Mfg. Co., Ltd.
Nishi-Nippon Aluminum Co., Ltd.
Nissei Sangyo Co., Ltd.
Panelal Nagoya Co., Ltd.
Sanbi Aluminum Industries, Ltd.
Techno Kogyo Kabushiki Kaisha
Toshin Press Co., Ltd.
Yamada Keikinzoku Co., Ltd.
Yodai Co., Ltd.
Greater Lebanon Hotel Enterprises, Inc.
Grupo Aluminio, S.A. de C.V.
Almexa, S.A. de C.V.
Aluminio, S.A. de C.V.
Inmobiliaria Aluminio, S.A. de C.V.
Halco (Mining) Inc.
Boke Service Company, S.A.
Boke Trading, Inc.
Compagnie Des Bauxites De Guinee (CBG)
Inversiones Araco Compania Anonima
Aco, Sociedad Anonima
Flotillera Oriental, Compania Anonima
Aco Inversora, S.A.
Aco, Sociedad Anonima
Aco, Sociedad Anonima
Aco Inversora, S.A.
Aco, Sociedad Amonima
Auto Cabimas, Sociedad Anonima
Inversora Baralt, C.A.
Inversora Central C.A.
Lago Motors, C.A.
Valfor, Sociedad Anonima
Arrendamientos Aco, S.A.
Auto Cabimas, Sociedad Anonima

Auto Caracas, Sociedad Anonima
Auto Oriente Maturin, S.A.
Auto Oriente, S.A.
Aco Alquiler S.A.
Automotriz Vigia S.A.
Agro Andina, S.A.
Automotriz Panamericana, S.A.
Inversora Central C.A.
Lago Motors, Compania Anonima
Tractosur C.A.
Centromotriz Zulia, C.A.
Cummins de Venezuela, S.A. (CUMMINSA)
Fabrica of Carrocerias Centauro, C.A.
Fabrica Nacional De Tractores Y Motores, S.A. "FANATRACTO"
Hidromex Venezolana C.A.
Inversiones Rialpe, S.A.
Inversora Baralt, C.A.
Inversora Orinoco, C.A.
Lamax S.A.
Aco Inversora, S.A.
Motoriente Ciudad Bolivar C.A.
Motoriente San Felix, S.A.
Motoservicio Ciudad Bolivar, C.A.
Motoriente San Felix, S.A.
Motoriente Ciudad Bolivar, C.A.
Motoservicio San Felix, C.A.
Talleres Unidos De Occidente, C.A.
Centromotriz Zulia, C.A.
Franquicias Unidas Occidente, S.A.
Talleres Unidos De Occidente, C.A.
Automotriz Veritas, S.A.
Flotillera Oriental, Compania Anonima
Talleres Unidos, C.A. (TAUNICA)
Administradora Maracay, C.A.

Amortiguadores, S.A.
Auto Cabimas, Sociedad Anonima
Auto Caracas, Sociedad Anonima
Aco Alquiler S.A.
Aco Alquiler Barquisimeto, S.A.
Aco Alquiler Occidente, S.A.
Aco Alquiler Oriente, S.A.
Flotillas Y Arrendamientos (Floarca), C.A.
Auto Oriente, Sociedad Anonima
Flotillera Oriental, Compania Anonima
Auto Oriente Maturin, S.A.
Flotillera Oriental, Compania Anonima
Autoservicio Maturin, C.A.
Grupo Covenal Mariara, C.A.
Indutrias Fairbanks Morse De Venezuela, S.A.
Inversora Baralt, C.A.
Inversora Central, S.A.
Automotriz Veritas, S.A.
Inversora Covenal, S.A.
Inversiones Auven, C.A.
Inversora Orinoco, C.A.
Aco Alquiler, S.A.
Aco Inversora, S.A.
Auto Oriente Maturin, S.A.
Auto Oriente, Sociedad Anonima
Motoriente Anaco, C.A.
Aco Alquiler Oriente, S.A.
Motoriente Ciudad Bolivar, C.A.
Motoriente El Tigre, C.A.
Aco Alquiler Oriente, C.A.
Motoriente San Felix, C.A.
Occidente Motors, S.A.
Inversora Veritas, S.A.
Lago Motors, Compania Anonima
Inmobiliaria Araure (INMAR, S.A.)

Aco Alquiler, S.A.
Cummins de Venezuela, S.A. (CUMMINSA)
Maquinarias Y Servicios Aco, S.A.
Maquinarias Y Servicios Aco, S.A.
Talleres Unidos, C.A. (TAUNICA)
Aco, Sociedad Anonima
Valfor, Sociedad Anonima
Aco Inversora, S.A.
Auto Cabimas, Sociedad Anonima
Auto Inversora Lamax, S.A.
Automotriz, Panamericana, S.A.
Automotriz Vigia, S.A.
Franquicias Unidas Occidente, S.A.
Industrial Vigia, S.A.
Inversora Central, C.A.
Inversora Baralt, C.A.
Lago Motors, C.A.
Tractosur, C.A.
Auto Cabimas, Sociedad Anonima
Aco Inversora, S.A.
Aco, Sociedad Anonima
Amuay Motors, C.A.
Auto Inversora Lamax, S.A.
Auto Servicio Cabimas, Sociedad Anonima
Franquicias Unidas Occidente, S.A.
Amuay Motor, C.A.
Automotriz Veritas, S.A.
Automotriz Veritas, S.A.
Talleres Unidos De Occidente, C.A.
Deformaciones Plasticas de Metales, C.A.
Forauto, C.A.
Aco Alquiler, S.A.
Agroven, C.A.
Grupo Covenal Mariara, C.A.
Inversiones Almonital, C.A.

Filtravedo, S.A.
Procesos Galvanicos, S.A. "PROGAL"
Sicam de Venezuela, S.A.
Fabrica National De Forros Y Accesorios Para Carros, C.A.
Enmar, C.A.
Inversiones Auven, C.A.
C.A. Venezolana de Produccion Renault
Constructora Venezolana de Vehiculos, C.A.
Filtravedo, S.A.
Inversora Covenal, S.A.
Metalmar, C.A.
Indutrias Mariara S.A. "INDUMAR"
Tupla, C.A.
Inversiones Metalurgicas, C.A.
Administradora Maracay, C.A.
Amortiguadores, C.A.
La Casa Del Amortiguador, S.A.
Auto-Amortiguadores Maturin S.R.L.
La Casa Del Amortiguador Barquisimeto, S.A.
Sinterizados Del Caribe, C.A.
Estampados Del Caribe, C.A.
Trefilerias Mariara, C.A.—TREMARCA
La Casa Del Amortiguador, S.A.
Tupla, C.A.
Tupla, C.A.
Inversiones Araco Compania Anonima
Inversora Baralt, C.A.
Inversora Central, C.A.
Lago Motors, Compania Anonima
Aco, Sociedad Anonima
Amuay Motors, C.A.
Franquicias Unidas Occidente, S.A.
Auto Inversora Lamax, S.A.
Agroven, C.A.
Aco Alquiler Occidente, S.A.

Indutrial Vigia, S.A.
Aco Inversora, S.A.
Aco, Sociedad Anonima
Auto Cabimas, S.A.
Auto Inversora Lamax, S.A.
Automotriz Panamericana, S.A.
Automotriz Vigia, S.A.
Franquicias Unidas Occidente, S.A.
Inversora Baralt, C.A.
Inversora Central, C.A.
Lago Motors, C.A.
Inversora Central, C.A.
Lamax, S.A.
Aco Alquiler Barquisimeto, S.A.
Occidente Motors, S.A.
Aco Alquiler Barquisimeto, S.A.
Inversiones Rialpe, S.A.
Inversiones Rialpe, S.A.
Mineraria Silius, S.p.A.
Fluorsid, S.p.A.
Moralco Limited
Norsk Alcoa A/S
A/S Skibsinvestering
Norsk Alcoa A/S
Mosal Aluminium
Elkem A/S & Co. (Partnership)
Shibazaki Seisakusho Limited
Shibazaki Metal Print Co., Ltd.
Oak Mountain Office Part, Inc.
n.v. hotelmaatschappij "TORARICA"
Swanal Limited